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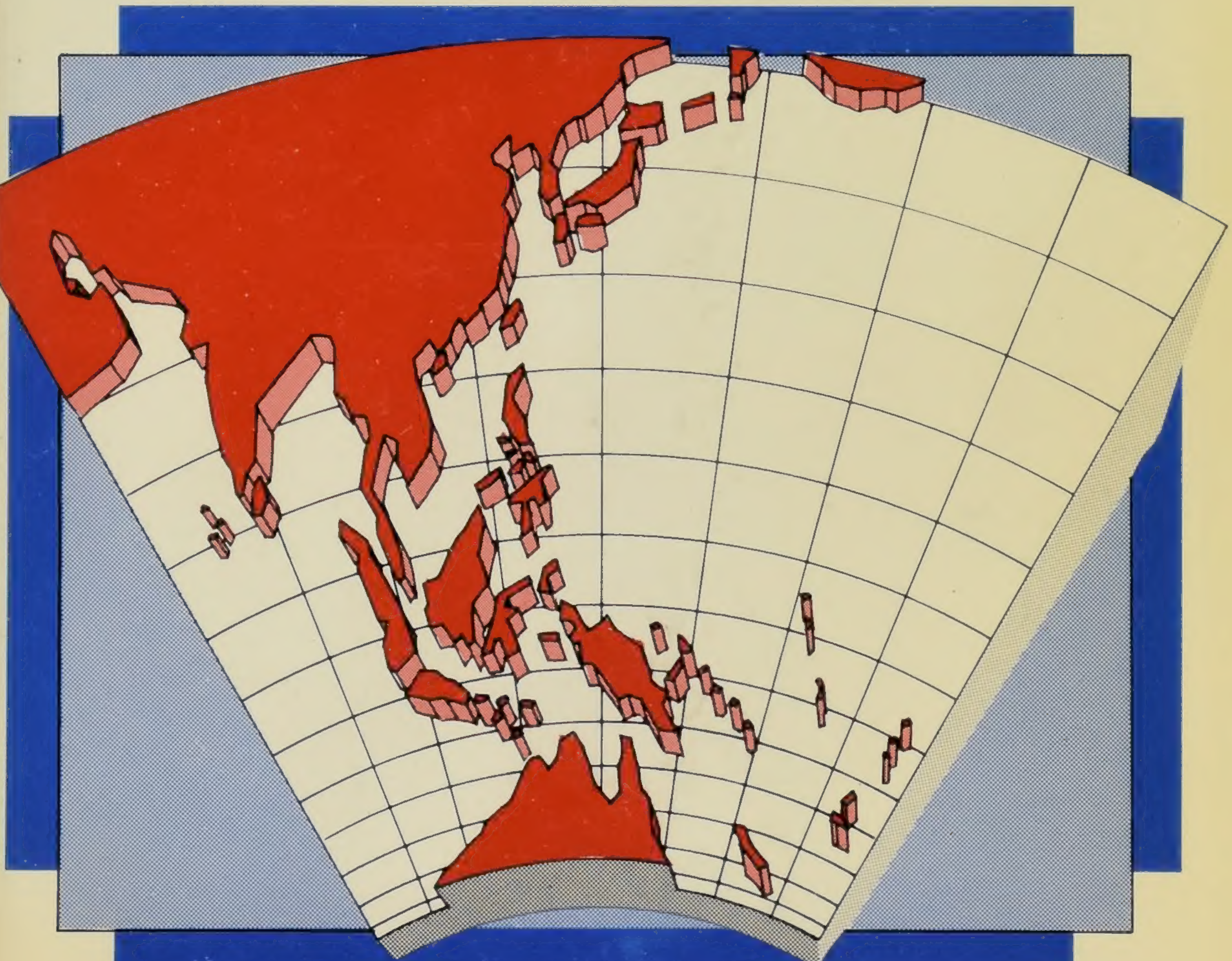
SERVICES IN ASIA AND THE PACIFIC

Selected Papers

Volume One



UNITED NATIONS CONFERENCE ON TRADE AND DEVELOPMENT

UNITED NATIONS DEVELOPMENT PROGRAMME

UNCTAD/ITP/51

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SERVICES IN ASIA AND THE PACIFIC: SELECTED PAPERS

Volume One

UNCTAD/UNDP TECHNICAL ASSISTANCE PROJECT
FOR SUPPORT TO ASIA-PACIFIC DEVELOPING COUNTRIES
IN MULTILATERAL TRADE NEGOTIATIONS

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Explanatory Notes

- References in the text and tables to "countries" are to countries, territories or areas as appropriate.
- The term "dollar" ($) refers to United States dollars, unless otherwise stated.
- The term "billion" signifies 1,000 million.
- Annual rates of growth and change refer to compound rates.
- Exports are valued f.o.b. and imports c.i.f., unless otherwise specified.
- Use of a hyphen (-) between representing years, e.g. 1965-1966, signifies the full period involved, including the initial and final years.
- An oblique stroke (/) between two years, e.g. 1980/81, signifies a fiscal or crop year.
- A dash (-) or a zero sign (0) indicates that the amount is nil or negligible.
- A plus sign (+) before a figure indicates an increase; a minus sign (-) before a figure indicates a decrease.
- The sign "na" stands for "not available".
- Details and percentages do not necessarily add up to totals, owing to rounding.

Abbreviations

ASA	Air Service Agreement
ASEAN	Association of South East Asian Nations
CAD	computer-aided design
CAE	computer-aided engineering
CAM	computer-aided manufacturing
CASE	computer-aided software engineering
CRS	computerized reservation system
DBS	direct broadcasting satellite
EC	European Community
ECSCAP	Economic and Social Commission for Asia and the Pacific
GATT	General Agreement on Tariffs and Trade
GDP	gross domestic product
GNP	gross national product
GNS	Group of Negotiations on Services
HDT	high-definition television
IATA	International Air Transport Association
IBRD	International Bank for Reconstruction and Development
ICAO	International Civil Aviation Organization
ILO	International Labour Organization
IMF	International Monetary Fund
INMARSAT	International Maritime Satellite Organization
INTELSAT	International Telecommunications Satellite Organization
ISDN	integrated services digital network
ITU	International Telecommunication Union
MFA	Multifibre Arrangement
MFN	most favoured nation
MFTS	multilateral framework for trade in services
MPEAA	Motion Picture Export Association of America
NBFI	non-bank financial institution
NGO	non-governmental organization

NIE	newly industrializing economy
OBU	offshore banking unit
OECD	Organisation for Economic Co-operation and Development
OTC	Overseas Telecommunications Commission
PC	personal computer
R & D	research and development
RBP	restrictive business practice
TNC	transnational corporation
UNCTAD	United Nations Conference on Trade and Development
UNCTC	United Nations Centre on Transnational Corporations
UNDP	United Nations Development Programme
UNESCO	United Nations Educational, Scientific and Cultural Organization
UR	Uruguay Round
USTR	United States Trade Representative
WIPO	World Intellectual Property Organization
WTO	World Tourism Organization

FOREWORD

UNCTAD's work on issues relating trade in services and the development process has intensified since 1987, when the Seventh Conference requested UNCTAD to analyse the implications of the issues raised in the context of trade in services. Much of this work has been carried out at the national, regional and interregional levels with UNDP support. Some of this has appeared in recent publications such as *Services and Development Potential: The Indian Context* (UNCTAD/ITP/22) and *Trade in Services: Sectoral Issues* (UNCTAD/ITP/26).

The UNDP Regional Bureau for Asia and the Pacific decided at the beginning of 1990 to increase the resources available to Project RAS/86/020 "Support to Asia and Pacific countries in Multilateral Trade Negotiations", in order to permit this project to undertake major studies on trade in services in the region. These studies are aimed at increasing understanding on the role of trade in services in the development of the Asia and Pacific region. They also seek to identify specific policy measures for stengthening the service sectors of developing countries in the region and for increasing their trade in services, both within and outside the region. Furthermore, these studies aim at enabling Asia-Pacific developing countries to participate more effectively in the Uruguay Round negotations on a multilateral framework for trade in services, and possible further negotiations on a sectoral or subsectoral basis.

This collection of papers represents a first step in this process. The sectoral studies have been prepared by a group of consultants, primarily from the Asia and Pacific region, who have addressed the above-mentioned issues in the context of specific service sectors in selected countries or groups of countries. These papers are the product of discussions at a seminar for ASEAN countries and at a regional seminar for Asia-Pacific countries held in Bangkok in May and August 1990 respectively. These seminars were organized by the MTN Project for the region, funded by UNDP and executed by UNCTAD in association with ESCAP. In designing the terms of reference for these studies, it was considered that it would be a more useful exercise to examine cer-

tain sectors and countries in relative depth, by experts with long experience in their respective fields and through intensive reseach methods including interviews and questionnaires, than to analyse the issues on a broader but more general basis. A series of boxes, prepared by the UNCTAD secretariat, supplements the information and arguments provided by the consultants in their papers. In addition, two papers prepared by members of the UNCTAD secretariat locate the specific sectoral and regional studies in the larger context of the Uruguay Round negotiations on trade in services.

Given the particular time of its publication, this volume concentrates on sectors which are currently being discussed in special sectoral groups in the Uruguay Round. (Unfortunately, telecommunications, shipping, and construction and engineering design could not be dealt with in this volume.) A second volume, examining a number of additional sectors, countries and trade policy issues, is currently under preparation. It is hoped that these papers will not only provide an original insight into the situation of selected service sectors in cerain Asian and Pacific countries, but also serve to stimulate future studies to be conducted under the Project as well as by governments, other international organizations and academic institutions.

STRENGTHENING SERVICE SECTORS IN ASIA AND THE PACIFIC: AN OVERVIEW

*Murray Gibbs, Michiko Hayashi and Udaya Kumar**

INTRODUCTION

In the past decades many of the economies of the Asia-Pacific region have prospered even when the economic growth of developing countries in other regions have been seriously affected by interrelated hardships like debt crisis, commodity market collapse and hyper inflation. One of the major factors of the high economic performance in the region has been the successful exportation of labour-intensive manufactured goods. What is less known is that the export of services has also played a significant role in the economic development of the region. Tourism, construction, labour services and some professional services became the important sources of foreign exchange earnings in the region. Recently, civil airlines in the ASEAN sub-region have also been expanding their shares of the international market. Perhaps, a more accurate way of describing the trend of the international economy in the region is that the trade in goods and services has been rapidly growing in parallel along with the economic development. The estimated figures based on the *IMF Balance-of-Payments Statistics* indicate that during the last decade trade in services in the region doubled, both for export and for import.

Observation on the balance-of-payments statistics by item indicated that the countries in the region became competitive on some services and also increased the reliance on foreign suppliers on other services.[1] The Republic of Korea, Maldives, Indonesia and Thailand

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1 A graphical presentation of balance-of-payments trends for several Asian countries

increased their foreign exchange earnings on travel while Bangladesh and Pakistan increased their deficit on the account. India and Singapore have maintained the favourable position on the account, and Malaysia remained as a most significant net-deficit country. Import of transport has been one of the major foreign exchange spendings in the service sector leaving most developing countries in the region in a continuous deficit position. The heavy reliance on foreign suppliers for transportation is particularly notable in India, Indonesia and Thailand. Only Singapore has been a major exception, enjoying a large surplus on the account over the decade due to earnings from shipping-related services. On the contrary, the export of labour services is an important source of foreign exchange earnings in the region. Among the countries, India and Pakistan were the most important countries for the export of such services being followed by the Philippines, Thailand and Bangladesh. For the trade in "other services", there was no general trend in the region. Indonesia had the largest deficit on this account during the last decade, and Malaysia had increased the import of such services significantly. On the other hand, the export of these services from the Republic of Korea and the Philippines have grown rapidly. Singapore has always been a major exporter of "other services" in the region, and at the same time it has been a major importer. Countries such as Nepal, Pakistan and Thailand have maintained their surpluses on the account although these have been small. For a few countries, data on trade in "management fees and film rentals" were available, and it indicated that the Republic of Korea has been increasing its surplus on the account. Further in-depth country level studies on the pattern of trade in services and the economic trend of individual countries may be necessary in order to understand the contribution of trade in services to the economic development in the region.[2]

There is no published data on foreign direct investment in the services sector *per se*. However, relevant studies[3] indicate that service

was included in *Services in the World Economy* (United Nations Publication, UNCTAD/TDR/8/Offprint).

2 No comparable figures are available for China. However, the service sector in China will be dealt with in Volume Two.

3 See, for example, UNCTC, *Foreign Direct Investment and Transnational Corporations in Services* (United Nations Publication, Sales No. E.89.II.A.1), and C.H. Lee and S. Naya, ed., *Trade and Investment in Services in the Asia-Pacific Region* (Boulder, Westview Press, 1988).

firms in developed countries, mostly originating from the United States and Japan, have invested in the countries in the Asia-Pacific region in the areas of financial, tourism, professional and retailing services. It is interesting to note that there is growing co-operation among regional firms, notably in the tourism sector, and that although many sectors are dominated by large enterprises from developed countries some of these companies are beginning to effectively compete with transnational corporations.

Although the overall economic growth in the region was favourable, it is also true that there exists a wide gap in the levels of economic development among the countries. The difference in GNP per capita among the countries in the region is quite striking. The countries of the lowest GNP per capita were Bangladesh and Nepal accounting $160 in 1987 and the highest ones were Hong Kong and Singapore, with $8070 and $7940 respectively. The Republic of Korea and Malaysia were in the next highest group amounting $2690 and $1810 respectively, while other countries ranged from $300 to $850. The statistics on national production indicated that the structure of the economies among the countries in the region differ to a great extent. Bangladesh and India still have a large agricultural sector while Singapore and Hong Kong are highly service-oriented economies. For other countries, industries and services have more or less equal importance in their economies. In the Pacific region, small island countries are vitally dependent on services (both imports and exports) such as air and maritime transport, telecommunications, labour services, tourism, etc. The widely different levels of economic development and structure among the countries in the region cleary indicates that each country must set different priorities and strategies for the trade and development of its service sectors.

The ongoing multilateral trade negotiations on services would imply that the international economy has gone into the era of trade liberalization in services, and competition in the international market will be further intensified. A recent UNCTAD publication[4] observed

4 See UNCTAD, *Trade in Services: Sectoral Issues* (United Nations Publication, UNCTAD ITP 26), particularly Murray Gibbs and Michiko Hayashi, "Sectoral Issues and the Multilateral Framework for Trade in Services: An Overview", pp. 1-48.

that competitiveness at enterprise level depends on attributes such as financial capacity, the ability to use telecommunication and information technologies effectively, networking ability, presence in a major market, appropriate government incentives, etc. Another such attribute might be the ability of firms to collaborate with other firms in order to enhance one another's competitiveness. The increasing trend of co-operation among transnational firms at intra and cross-sectoral levels testifies to this. Such co-operation aims at strengthening competitiveness by combining competitive edges of individual firms in distribution and information channels, market intelligence and financial capacity, and as a result makes entry to the international market more difficult for new entrants. Such co-operation would seem to become an inevitable competition strategy for a growing number of service sectors. In such an environment, regional co-operation such as in the tourism sector referred to above might become more important than before in improving the competitiveness of service sectors in the region.

The concluding paper in this volume examines in detail the main thrust of developing-country objectives in the negotiation of a multilateral framework for trade in services and the Uruguay Round.[5] The stated objectives of the Montreal Ministerial Mid-Term Review were to strengthen the domestic service sectors of developing countries, increase their efficiency and provide developing countries' service suppliers with effective access to markets, as a means of increasing the participation of developing countries in international trade in services. Developing countries are currently pressing strongly for the inclusion of concrete provisions in the multilateral framework being negotiated, in order to incorporate these principles into meaningful multilateral obligations. An important responsibility in this area also falls upon the governments of the region themselves to formulate and implement the policy measures necessary to strengthen the position of their service suppliers in regional and world trade in services. The Uruguay Round, depending on the success of developing countries in effectively protecting their interests, could either promote or impede the ability of developing countries in the Asia and Pacific region to attain these objectives. The following paragraphs summarize the types of problems that will

5 Murray Gibbs and Mina Mashayekhi, "The Main Issues in the Negotiation of a Multilateral Framework for Trade in Services", elsewhere in this volume.

have to be addressed by policy makers in these countries in pursuit of these objectives.

I. ACCESS TO TECHNOLOGY AND TRAINING FACILITIES

For most of the Asia-Pacific countries, the availability and application of advanced technology remains crucial for gaining competitiveness in several service sectors. This applies not only with respect to the so-called new services which are in a sense a product of information and telematic technologies, but also in many cases to what have generally been considered as traditional services and are coming to be increasingly reliant on, and transformed by, new technologies. The increased participation of developing countries in the Asia and Pacific region in international trade in services, will be largely a function of their ability to meet the challenge of updating their technological base in order to face global competition in services.[6]

One particular example of how the competitiveness of Asia-Pacific countries having been adversely affected by technological advancement is that of shipping. The increasing use of containerization and transhipment since the 1970s have meant that heavy capital investment, computerized control of operations, new forms of organizational and management techniques, and access to modern telecommunications technology are essential for retaining or gaining competitiveness in liner shipping. While the share of developing countries was 27.6 per cent in the world's tonnage of general cargo ships in 1988, the figure for container ship tonnage was only 13 per cent.[7] The participation of Asia-Pacific countries such as India, Malaysia, and Thailand in containerized trade is modest, while a large part of the total outgo of cargo from these countries is containerized. An illustration of this trend is that, as a consequence of the increasing use of

6 The importance of technology in this respect has been discussed in previous UNCTAD documentation, e.g. *Services in the World Economy* (United Nations Publication, UNCTAD/TDR/8 Offprint), *Trade in Services: Sectoral Issues* (United Nations Publication, UNCTAD/ITP/26).

7 L.M.S. Rajwar, "Trade in the Shipping Sector: India, Thailand and Malaysia", *Services in Asia and the Pacific*, Volume 2 (United Nations Publication, forthcoming).

transhipment ports, services to several smaller ports in Malaysia have been disrupted.[8] Some countries have also tried to take advantage of this change in the patterns of shipment. Fiji has attempted to generate more traffic by offering competitive rates to get shippers to use its facilities for transhipping cargo and thus to become the transhipment centre of the Pacific Islands.[9]

In some other traditional services, e.g. insurance, the use of advanced technologies have resulted in a segmentation of the domestic market into a dual structure. In the Republic of Korea, competitiveness among large firms is determined by expertise, knowledge and networking, whereas among the small firms the determining factors are price, language ability and cultural contact.[10] There is not much competition between the two segments, the former is directed toward large corporations and transnational clients, the latter is directed at smaller domestic clients. This two-tier phenomenon can be found in business services as well, such as advertising, accounting and market research.[11] In his paper on the insurance sector in Korea, Un Hoe Park also argues that Asia-Pacific countries require technical assistance from developed countries in such aspects as product design, rating industrial risks, and in reinsurance capacity. Networking remains a crucial factor in the competitiveness of domestic firms in relation to this.[12]

One of the major problems faced by firms from the region in expanding their exports of media products also relates to the availability of technology. Technology and the availability of skills are essential for enhancing the marketability of media products. Overcoming the language barrier would require facilities and resources for subtitling and dubbing into the language of the destination country. Furthermore, the technical quality of the print is a crucial determinant of marketability. The emergence of television and video technologies has meant that to become competitive in the provision of media services in these forms, countries from the region may need enormous infrastructural invest-

8 *Ibid.*

9 Yee Che Fong, "Trade in Services in Pacific Island Countries", elsewhere in this volume.

10 Un Hoe Park, "Trade in Insurance in Korea", elsewhere in this volume.

11 Sieh Lee Mei Ling, "Professional Services in Malaysia", elsewhere in this volume.

12 Park, *op. cit.*

ment in updating their transmission technologies. This would include the installation of fibre-optic cables, cable television and high definition television.[13]

However, as Dorothy Riddle points out, the current multilateral trade negotiations and the possibility of liberalization of services trade also present the Asia-Pacific countries with opportunities for gaining competitiveness in services, relying on a strategy based on human resources development and infrastructure management.[14] Many of the Asia-Pacific countries have a literate work force with access to good public education. However, the lack of an adequate number of specialized trained personnel has been noted by several analysts as an impediment to the growth of several sectors. This includes various service components of the tourism sector such as hotel industry and travel services, business services such as advertising and accounting, insurance and other financial services, and perhaps most importantly, computer-related services. For example, tourism is becoming important for a number of countries, and a number of resource-poor countries such as some Pacific Island countries depend heavily on tourism for their foreign exchange earnings. However, the development of this sector, with all the various service activities it involves, remains constrained by the lack of capital funds, expertise, and inadequate development of transport, telecommunications, and advanced technologies.[15]

It can be seen that training opportunities need to pertain to different levels of competence. For example, in the case of software and computer-related services, some Asia-Pacific countries such as India and the Philippines need to enhance the rapidity of their educational systems in responding to the growing needs of the industry. This involves the provision of better higher education facilities in computer technology, along with the provision of adequate equipment as well as funding. Singapore and, to a lesser extent, the Republic of Korea seem

13 Malati Tambay Vaidya, "Trade in Media Services: Six Asian Countries", elsewhere in this volume.

14 Dorothy Riddle, "Fostering the Growth of New Service Exports from Developing Countries", *Services in Asia and Pacific*, Vol. 2, *op. cit.*

15 Yee, *op. cit.*

to have responded to this problem in an effective manner.[16] In some other cases, the entrepreneurs need to be made aware of trade possibilities in certain sectors through workshops and training programmes. Entrepot trade in Sri Lanka would be a case in point. This could help in taking advantage of the geographical position of the country for developing trade in this sector.[17]

The training of employees in advanced skills and techniques remains indeed the most crucial form of human resources development in several sectors. In certain cases, intergovernmental co-operation has responded effectively to this challenge. For example, a training programme of hotel workers, sponsored by the European Community in the ASEAN countries has been much welcomed.[18] In general, however, the main sources of transfer of technology have been through arrangements such as joint ventures or networking with foreign firms. In business services in ASEAN, training by foreign experts brought from affiliates has been found to constitute an effective form of technology transfer. However, contracts concerning hotel management are often vague about training and the specific terms under which it will be carried out. In this situation, it may be useful for governments to tie tax incentives or market access for firms which implement approved company training programmes or to encourage in-company training programmes with subsidies. Thierry Noyelle identifies joint ventures as an effective mechanism for upgrading domestic labour skills in software services.[19] Here, technology transfer is intricately linked to issues of market access and the ability to move personnel to foreign markets, since assignments abroad serve as a major means of upgrading skills. Modalities for the training of personnel from developing countries in developed countries would also need to be worked out more effectively in this sector. Overly stringent intellectual property protection poses a particular problem as it can impede a wider dissemination of technology and skills. However, adequate protection is necessary to stimulate the

16 Thierry Noyelle, "The Growth and Internationalization of Computer Software and Services in Five Developing Asian Countries", elsewhere in this volume.

17 Anton Fernando, "Entrepot Trading Services in Sri Lanka", *Services in Asia and the Pacific*, Vol. 2 (United Nations Publication, forthcoming).

18 Chow Kit Boey, "International Tourism in the ASEAN Region", elsewhere in this volume.

19 Noyelle, *op. cit.*

domestic production, in software in particular. It has been suggested that one possible solution for this could be the negotiation of site licenses for the use of specific software in specific countries. This has already been done in at least one country in the Asia-Pacific region.[20]

As has been noted below, transnational corporations dominate international markets in most service sectors, and the challenge facing countries of the region is to devise effective mechanisms to ensure that TNCs function as effective agents of transfer of technology. The transfer of technology potential of TNC activities differs greatly as between service sectors. For example, the United Nations Centre on Transnational Corporations found that in Brazil, the activity of TNCs in telecommunication services involving transborder data flows did not have any major impact on the country's technological capacity.[21] In financial services, the study noted reluctance on the part of transnational banks to use new financial instruments in Malaysia and Korea.[22]

Media services, as a result of the distance between the locations of production and distribution, is a sector where trade does not normally entail the transfer of technology.[23] Special modalities need to be devised in this sector to enable firms from the region to access advanced technologies prevalent in the developed countries. Co-production is one area where specific measures for the training of personnel could be explored.

On the other hand, as has been highlighted by both Thierry Noyelle and Sieh Mei Ling, the potential for technology transfer is most prominent in the sector of professional and business services. The training of local personnel is inherent in the effective operation of foreign professional/business service firms in Asia and the Pacific which require major training efforts to keep up with constant changes in soft technology. Job-hopping is one of the ways in which their soft technology diffuses in many sectors. Since the training material has to be adapted to differences of location on account of the different laws and

20 *Ibid.*

21 UNCTC, *Transnational Corporations, Services and the Uruguay Round* (United Nations Publication, Sales No. E.90.II.A11), p. 57.

22 *Ibid.*, p. 133.

23 Vaidya, *op. cit.*

other factors, there is an increasing decentralization of training programmes. For many years, the American International Group in the Philippines implemented a training programme for its managerial staff in Far East offices which resulted in a significant turnover of the trained staff as dissemination of skills and knowledge to the economy of the country. This provoked a decision by the company to end its training programme in the Philippines,[24] demonstrating the need for developing countries of the region to include the maintenance of such training programmes among the conditions for access for such firms. In any case, the policy of higher salaries and fewer personnel in TNCs can make it difficult for domestic firms to bid away their staff, and the foreign corporations would not seem to be threatened in this respect.

A few Asia-Pacific countries, notably Singapore, are in a position to attract foreign information-technology professionals by providing attractive wages. In some other countries like India, there has been an active encouragement by the government, towards private firms bringing back expatriate citizens working in senior positions in the computer industries abroad.[25]

Indeed, a major problem faced by many developing countries in improving their service imports is the lack of adequate development of technological infrastructures. In India, for example, the domestic market for software services remains hindered in its development by the relatively small installed base of computers. The lack of adequate equipment can seriously impair the development of competitive and advanced software services.[26] Some countries, such as the Republic of Korea, have turned to computerization in the 1980s to enhance productivity when the comparative advantages in terms of labour costs became eroded by the rapid rise in wages. Singapore has actively promoted a computerization programme in both the public and private sectors. Over recent years, India has relaxed or removed all regulations concerning the establishment of subsidiaries of foreign computer firms and their importation of equipment so long as the subsidiaries production of services (i.e. software) is solely for export. In the Republic

24 UNCTC, *Transnational Corporations, op. cit.*, p. 134.

25 Noyelle, *op. cit.*

26 *Ibid.*

of Korea, the government seems to actively encourage joint ventures and other forms of linkages between global firms and local companies.[27]

A similar problem, no less important, concerns the development of adequate telecommunications infrastructures. In the context of the increasing importance of telematic technologies in determining international competitiveness in trade, especially in services, many developing countries are faced with a paradoxical situation. On the one hand, as Riddle says, this context provides them with the opportunity to "leap frog" in the development and delivery of advanced services.[28] Some Asia-Pacific countries have already accessed the international markets in certain sectors where services can be delivered through telecommunications networks. The Republic of Korea and the Philippines have developed a degree of competitiveness in remote data processing, and the software development in India can make use of telematic technologies to transmit orders as well as products to the United Kingdom and to Europe.[29] It is also argued that the creation of special telecommunications trade zones or teleports might enable developing countries to capture a small portion of the world's data services markets. Since teleports are located near satellite transponders, the interconnection with national networks is rendered unnecessary.[30]

While all these possibilities appear attractive from the point of view of the potential market entry of developing-country firms, they also demand a reorientation of telecommunications policy in most Asia-Pacific countries. Enhancing the telecommunications infrastructure for the needs of transborder delivery of services would require the installation of fibre-optic cables in the urban centres of many of these countries.[31] This might prove in most cases to be at the expense of extending the telecommunications network beyond the urban areas. The restructuring of the objectives of telecommunications ser-

27 *Ibid.*

28 Riddle, *op. cit.*

29 Noyelle, *op. cit.*

30 Riddle, *op. cit.*

31 See G. Russell Pipe, "Telecommunications Services: Considerations for Developing Countries in the Uruguay Round Negotiations", in UNCTAD, *Trade in Services: Sectoral Issues, op. cit.*, pp. 49-111.

vices and the subordination of their public utility function to their trade-facilitating function might be unacceptable to many countries in the region from the point of view of long-term development goals.[32]

II. MARKET ENTRY AND TRANSNATIONAL CORPORATIONS

A recurrent issue in the following studies concerns the problems that developing-country firms face in gaining effective access to markets in several service sectors. Transnational firms based in developed countries dominate most of the domestic service sectors in developing countries. In tourism, for example, the inbound tour market to ASEAN countries is dominated by big firms linked to TNCs.[33] Thus smaller domestic firms are disadvantaged in the absence of linkages with tourist-generating country firms. This is further aggravated by the asymmetries in access to information networks and reservation systems, which we shall examine in the next section. Foreign dominance can also be seen in the hotel sector in ASEAN, in conjunction with increasing prevalence of vertical integration linking hotel chains to airlines, tour operators and travel agents. Sixty per cent of the foreign hotel chains in ASEAN are linked to domestic firms through management contracts.[34] Recently, strong competition from domestic hotel-management firms has resulted in a weakening of the bargaining position of TNCs vis-à-vis domestic hotel owners and this has resulted in more favourable terms in management contracts for the latter. Some of the ASEAN tour-operating firms have entered the inbound market by first building their presence in the outbound traffic market, and then by establishing offices abroad with migrated nationals.[35]

Various service sectors in the Pacific Island countries also show a pronounced foreign dominance. It has been argued that the dominance of foreign firms in the internal transport of these countries has resulted in the provision of transport services tailored to the needs

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32 *Ibid.*

33 Chow, *op. cit.*

34 *Ibid.*

35 *Ibid.*

of a foreign clientele rather than to those of the local population.[36] In advanced information-related technologies, there are foreign suppliers who hold exclusive marketing rights in the Pacific area. Australia and New Zealand are major investors in several service sectors in these countries. As a result of several factors including trade, telecommunications facilities connecting the Pacific Island countries with Australia and New Zealand are better than the facilities that exist within individual Pacific Island countries and between them.[37] Many of these islands rely on foreign suppliers for telecommunications facilities, with the OTC currently bidding to manage or operate networks on a joint-venture basis. Many Asia-Pacific countries are also concerned about the questions of sovereignty and territoriality implicit in this issue.[38]

In business services in ASEAN, once again the dominance of foreign firms was apparent: the two largest market research firms in each country are foreign-owned, and only two among the top advertising firms are locally owned.[39] In accounting, despite prohibitions on foreign partnership in countries other than Singapore, there is strong foreign presence in the form of affiliations. In competing with transnational firms, domestic firms are often faced with a serious disadvantage since the latter cannot easily gain the economies of scale and scope, because of the smallness of domestic markets. As a consequence, they often do not attain the critical mass to venture abroad.[40]

As has been pointed out in several studies, in the absence of adequate prudential regulations at the national and multilateral levels, the activities of transnational corporations can result in welfare losses for host developing countries. In terms of balance of payments, this can take the form of adverse effects arising from repatriation of profits, intra-firm transactions, cost-sharing, purchases from abroad, etc.[41] In banking services, there has been repatriation of excess capital as well as profits, and insurance firms have been seen to reinvest premium reven-

36 Yee, *op. cit.*

37 *Ibid.*

38 See Pipe, *op. cit.*, and Albert Bressand, "Access to Networks and Service Trade: Uruguay Round and Beyond", in UNCTAD, *Trade in Services, op. cit.*, pp. 215-47.

39 Sieh, *op. cit.*

40 *Ibid.*

41 UNCTC, *op. cit.*

ues outside developing countries. There could be other negative effects too such as lack of concern for the specific development priorities and cultural preferences of the host country, boom-and-bust cycles in employment generation in the case of construction firms, etc.[42]

An extremely important problem posed by the dominance of transnational corporations for domestic service firms in relation to market entry concerns their anti-competitive or trade-restrictive practices.[43] Intra-firm networks in many service sectors often convert possible competition into co-operation as foreign-owned or foreign-associated firms will not consider exporting to a country where affiliates are present. This creates the perverse result that transnationalization stifles competition, although it must be borne in mind that exports may take place in the form of support of one affiliate to another. This has been observed in the case of foreign-affiliated accounting firms in ASEAN.[44] As we noted in relation to the question of technology, the market in many developing countries is segmented into larger and smaller firms, the larger firms often affiliated to foreign firms. The dominance of transnational corporations or their affiliates can seriously restrict the amount of competition in the domestic service sector, since assignments of the parent firm in the region are usually given to the affiliate. Often TNCs have global contracts with other TNCs to supply services (e.g. accounting, advertising), thus undermining the potential market for services arising from the presence of TNCs. These phenomena prevent the smaller local firms from gaining competence and efficiency, since such gains are largely dependent on their having access to more demanding assignments, and to the major transnational clients.[45]

Media services is an area where Asia-Pacific countries have demonstrated considerable productivity. More than half of the films in the world are produced in the region. However, this share is far from reflected in the international trade in media products, which is domi-

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42 *Ibid.*

43 See Philippe Brusick, Murray Gibbs and Mina Mashayekhi, "Anti-Competitive Practices in the Services Sector", in UNCTAD, *Uruguay Round: Further Papers on Selected Issues* (United Nations Publication, UNCTAD ITP/42), pp. 122-56.

44 Sieh, *op. cit.*

45 *Ibid.*, and Noyelle, *op. cit.*

nated by developed market-economy countries, especially the United States.[46] The dominant position of market power exercised by cartels in this area seem to have hindered the possibility of enhancing Asia-Pacific exports in this sector. Since United States has the largest market for media products, it is easier for firms from there to supply additional copies of media products at relatively cheaper costs. This, combined with control over distribution channels in a large number of countries has aggravated the difficulty of new entry into the sector.[47]

In financial services, many Asia-Pacific countries have allowed an increasing number of foreign banks to operate in their countries, often under certain restrictions with regard to scope of operation, ownership, etc. It is felt that the selective introduction of transnational banks into these countries can lead to the expansion of banking networks in these countries and to increased competition in certain submarkets for particular banking services, as well as to the transfer of skills. In some countries, they are even subject to less stringent requirements than domestic banks. For example, in India, foreign banks are exempt from the obligation to open branches in rural areas or to lend to small, frequently high-risk borrowers at concessionary rates of interest. In the Republic of Korea, they are exempted from requirements to support government bond issues and to devote substantial proportions of their lending to specific sectors, while, at the same time, they enjoy tax privileges. In Taiwan, Province of China, regulations on the upper lending limit is less strict towards foreign-owned banks.[48]

However, several developing countries in the region are apprehensive about opening their domestic banking sectors to the operation of transnational banks. Their worries mainly concern the competitive strength and governability of these banks. Many transnational banking networks have demonstrated their capacity to evade taxes, to facilitate capital flight and to conceal aspects of their operations from the regulatory authorities. There is also the possibility that they might practise price discrimination to squeeze or stifle indigenous competitors. Fur-

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46 Vaidya, *op. cit.*

47 Susan Christopherson and Stephen Ball, "Media Services: Considerations Relevant to Multilateral Trade Negotiations", in *Trade in Services, op. cit.*, pp. 249-308.

48 Andrew J. Cornford, "Notes on a Possible Multilateral Framework for International Trade in Banking Services", in UNCTAD, *Uruguay Round, op. cit.*, p. 165.

thermore, foreign banks can use their access to external sources of funding in order to evade the impact of domestic monetary policies designed by host countries to restrain monetary expansion. Many developing countries in the region may also feel that classical techniques of monetary policy that are used in developed market-economy countries are less effective in countries which lack markets for liquid, short-term financial assets.[49] Here again, questions of trade seem to be intricately bound with questions of sovereignty and of autonomy of policy-making.

Some developing countries in the Asia-Pacific region encourage joint ventures rather than foreign direct investment as such, in order to ensure harmonization between business interests and overall development objectives. In many ASEAN countries such as Indonesia, there is a conscious encouragement of joint ventures in the banking sector in specific cities rather than full-scale liberalization. This can also be seen in a number of other sectors. This is particularly relevant in the light of findings that business service TNCs in some countries inordinately rely on expatriates for managerial jobs. This is indeed less the case with local partnerships, but nonetheless prevalent in spite of legal structures. However, if well-managed, such joint ventures can provide the needed expertise as well as international recognition to service firms from developing countries. In the construction joint ventures in Korea, attempts were made to ensure that the Korean firm was in the lead position, and this has proved important for successful transfer of technology in this sector.[50]

In software services, many Japanese firms have subcontracting relations with Filipino firms. Getting market entry in this area is crucially dependent on technical capacity. This in turn is dependent on obtaining access to complex assignments abroad and to advanced technology. Maintaining an office in a developed country presents financial difficulties for many developing-country firms. This is especially

49 *Ibid.*, p. 179.

50 Yehia Soubra, "Construction and Engineering Design Services: Issues Relevant to Multilateral Negotiations on Trade in Services", in UNCTAD, *Trade in Services, op. cit*, p. 199. See also Riddle, *op. cit.*

the case in software services where some lead time is required before a proper business presence can be established.[51]

Singapore software firms have made considerable success in penetrating the international market. Many of the top firms have sales and production offices overseas, and firms which specialize in turnkey projects have developed networks of overseas offices, mostly throughout the region. However, due to the shortage of information technology trained personnel, Singapore firms overseas have tended to concentrate on activities that mainly utilize local labour.[52]

III. ACCESS TO INFORMATION NETWORKS AND DISTRIBUTION CHANNELS

Closely related to the question of market entry and market concentration, and as has been recognized in the Uruguay Round context, difficulties in obtaining access to information networks and distribution channels also present developing-country firms with impediments in effectively participating in international trade in services, or from gaining in real terms from possible liberalization therein. This is all the more significant in the context of increasing use of telematic technology in the delivery of services. This and the consequent problems related to networking can be seen in several sectors such as air transport, banking, business services and computer-related services.[53]

Computerized reservation system (CRS) is one example of the problems posed by networking. The use of CRSs greatly facilitates the process of reservation and has become essential to travel agents. However, it has been argued that the operation of CRSs often involve a number of biases. The best known among them is display bias - i.e. the practice of arranging flight information on a CRS display to favour CRS host carriers and to make flight information of competing non-host airlines difficult to find.[54] It is estimated that about 85 per cent of

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51 Noyelle, *op. cit.*

52 *Ibid.*

53 Bressand, *op. cit.*

54 John Roland Miteus, Jr., "European Community Regulation of Airline Computer

the reservations are done by travel agents on the first screen and two-thirds on the first lines of the first screen.[55] This means that the use of carrier identity as a means of ranking flights can deprive non-host carriers of potential passenger revenue. There are other biases too possible in CRSs, arising from the vendor control of flight information as well as from the contractual relations between CRS vendors, non-host carriers and subscribers. These include the manipulation of the flight information displayed, dicriminatory booking charges, and requirements of subscriber loyalty.[56]

The United States reservation market is dominated by the Sabre CRS (owned by American Airlines) while the European markets are mainly dominated by Galileo and Amadeus systems. Reliance on CRSs owned by developed-country competing airlines may place developing-country airlines at a serious disadvantage. Though many developing countries are members of Gabriel II, a CRS owned by the airlines co-operative SITA, this system is regarded as inadequate in competing with the big systems of developed-country airlines.

In South-East Asia, a CRS named Abacus, based in Singapore and involving Cathay Pacific, Singapore Airlines, Malaysia Airlines, China Airlines and Philippine Airlines, is being developed. Abacus is connected to Amadeus and is expected to operate from mid-1991. There are other kinds of networking advantages also that could arise from the long-term use of CRSs. As analysts point out elsewhere in this volume, they facilitate the creation of conglomerates of airlines that provide their services through a combination of carriers from various airlines.[57] If this arises, competition between individual airlines will be replaced by that between systems of airlines and, as a consequence, non-member airlines will be increasingly at a disadvantage.

A wider problem is raised by the increasing importance of networking, which is apparent in several sectors. In civil aviation, the economies of networking have generated issues including the allocation

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Reservation Systems", *Law and Policy in International Business*, Vol. 21, No. 1 (1989), pp. 93-118.

55 Bressand, *op. cit.*, p. 240.

56 Miteus, *op. cit.*

57 Christopher Findlay and Peter Forsyth, "ASEAN Interests in Air Transportation Services in the Uruguay Round", and elsewhere in this volume.

of capacity on international routes and access to traffic originating at domestic points. Asian carriers have expressed concern about their bargaining power vis-à-vis European airlines in this connection. Furthermore, networking, in combination with vertical linkages involving tourism firms and airlines are likely to lead to the creation of systems of firms or consortiums. There are already a number of strategic alliances in the international air transport industry that point in this direction. Some South-Asian airlines have already developed such alliances and agreements. In addition to the co-operation in Abacus CRS, Thai International has marketing agreements with SAS, and Singapore Airlines has swapped shares with Delta Airlines and Swissair, as part of a link-up to offer a more efficient global network to consumers.[58] In the context of increasing airport congestion, the system of bilateral air service agreements and possibilities for improving market entry depend to a large extent on rules on access to networks and ancillary services.

For several Pacific Island countries for whom tourism and allied services are a major source of income, international civil aviation networks present some important problems. The viability of tourism is dependent on the services of international airlines that operate from source countries to the Pacific islands. The rationalization of services between Australia, New Zealand, North America and Japan has resulted in a drastic reduction of *en route* touchdowns in Pacific Island countries.[59] Though many of these countries have attempted to solve these problem through the development of national airlines, they are yet to make an inroad into the aviation sector in the Pacific region, currently dominated by Qantas and Air NZ. Moreover, the national airlines of Pacific Island countries have only terminating rights in Australia and New Zealand, while Qantas and Air NZ have fifth-freedom rights in the Pacific Island countries, enabling them to pick up passengers from there and take them to destinations in North America or Japan.

In business and financial services too networking plays an increasingly important role. The introduction of new financial instruments and the use of advanced technologies in communication available

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58 *Ibid.*

59 Yee, *op. cit.*

to firms networked to foreign firms seem to create a two-tier market, i.e. a few large firms supplying transnational clients and large domestic firms, and a large number of small firms supplying small and medium-size domestic enterprises.[60] If developing-country exports in these services are to increase, they would need to have access to these networks and distribution channels for the delivery of services. Thierry Noyelle, elsewhere in this volume, points out that the current software distribution system is dominated by the big hardware manufacturers and a few very large independent software houses.[61] Most of these firms also sell their own applications and often there can be discrimination in favour of these products. When a small, independent software house succeeds in establishing a successful product, the big distributors, when so permitted, will not hesitate to buy it outright rather than compete with it. This is further complicated by the discrimination practised by vendors of equipment, in favour of large systems integrators as opposed to small.

Access to distribution channels is an important source of competitiveness in media services markets as well. As we have already noted, since additional copies of media products can be made at a fraction of the original cost of production, and since their value is a function of where and when they are displayed, control over distribution becomes crucial in this area. The dominant position of cartels in this area has hindered effective trade liberalization here. This has taken the form of lack of availability of viewing time for products from other countries in cinemas as well as in television. It has been argued that some Asia-Pacific countries have come under bilateral pressure from the home countries of such cartels to allow the establishment of distribution channels directly owned by the cartels.[62]

60 This phenomenon has also been observed in Latin America, see Cesar Penaranda, "El Comercio Internacional de Servicios Profesionales: Situación y Perspectivas para América Latina y el Caribe en la Ronda Uruguay", UNCTAD/ESCAP/UNDP, forthcoming publication.

61 Noyelle, *op. cit.*

62 Vaidya, *op. cit.*

IV. FINANCIAL STRENGTH

Service firms from countries in the region face a further problem in accessing international markets, by virtue of inadequate financial strength. In some traditional sectors that have been transformed by advanced technologies, this has taken the form of enormous infrastructural costs necessary for technological updating. We have examined some examples of this earlier in this paper. In shipping, for example, the replacement of older vessels, containerization of cargo, modernization of cargo-handling facilities - all these require huge investments which many shipping companies in the region find difficult to afford.[63] The two-tier structure that Sieh Lee Mei Ling discerns in the business service sector in ASEAN countries is not only determined by technology, but by financial strength as well.[64] The financial weakness of small and medium-sized firms in travel services, hotel and tour operating services have meant exclusion from certain networks and certain markets. A larger problem that relates to financial strength and technologies is the difficulty that we have already noted on the part of several countries in the region in updating telematic infrastructures. This can affect the competitiveness of domestic firms in a number of sectors.

Many Asia-Pacific countries are bound to find financial strength as a crucial factor in competing with transnational service corporations. This is especially true in relation to financial services, where transnational banks have much easier access to funds. The superior strength of foreign banks may enable them to stifle indigenous competitors through price discrimination between markets in different countries.[65]

In computer software and services, several developed-country firms are heavily subsidized by various government projects. This is true of some Asia-Pacific countries too, but studies have pointed out the need for greater financial incentives. Funding also needs to be made

63 Rajwar, *op. cit.*

64 Sieh, *op. cit.*

65 Cornford, *op. cit.*, p. 170.

available at adequate scale, in order to promote personnel development through enhanced computer programming and computer science programmes in schools and universities. Availability of appropriate financial resources has also affected the kind and range of computer equipment available in many countries. As mentioned earlier, software development in countries such as India has been hindered to some extent by the small-installed base of computers in the country.[66]

Another problem in this sector relates to the high cost of establishing a foreign presence in developed countries. As Noyelle points out, even though barriers to entry in the economic sense of the term are very few in the software industry, the cost of sustaining a presence in a major developed country is likely to be very high for a firm from a developing nation, unless the foreign office can become revenue producing almost instantly. This is rather unlikely, especially in areas such as packaged software, which require some lead time before sales are generated. We have already discussed the implication of financial strength in the competition between small and large software firms, while discussing issues of market access.[67]

Another aspect of financial weakness relates to economies of size and scale. In professional services, Sieh Lee Mei Ling identifies a number of economic hindrances that are relevant in this context.[68] The first among them concerns the smallness of the domestic market which can prevent domestic firms from attaining economies of scale. Furthermore, the situation is aggravated by the low absolute value of net revenue obtainable from a small domestic market. This does not yield attractive margins for entrepreneurship. Examples include the small commission derived from media expenditure in Indonesia and the lack of entrepreneurial activity in Singapore advertising. Another problem relevant in this context is the impact of currency differentials on the competitiveness of firms.[69]

In civil aviation, where airlines from the newly industrializing countries from East Asia have been less constrained by access to fi-

66 Noyelle, *op. cit.*

67 *Ibid.*

68 Sieh, *op. cit.*

69 *Ibid.*

nance, many other developing countries face financial difficulties in buying aircraft and updating their airport infrastructures. Even though the industry is not as capital-intensive as is generally believed (insofar as capacity-related costs are only a small proportion of the total costs),[70] the cost of buying aircraft can be very high. Leasing aircraft is an option adopted by many national airlines from the region in order to overcome limits of funding.

V. MOVEMENT OF PERSONNEL

Most developing countries of the region have a comparative advantage in the supply of unskilled and certain kinds of skilled labour, on account of their cheaper wages. However, they find it difficult to take advantage of this in actual international trade in labour services, because of a large number of restrictions prevalent in developed countries in relation to the movement of personnel. Visa and workpermit restrictions are among these. This has affected the prospect of growth of developing-country firms in a number of service sectors, where trade involves cross-border mobility of labour. Software services are a case in point, particularly as "body-shopping" is an important means of delivery of software services.[71] Immigration restrictions have impeded the growth of such trade from many Asia-Pacific countries who have been trying to build an international presence in this sector relying on their skilled labour force. In India's computer consultancy exports, 80 per cent has been on-site, and work permit restrictions imply major losses in potential business for the country's software firms.[72] These restrictions can affect training and after-sales service as well. Unless adequate means for the short-term cross-border mobility of personnel can be effectively achieved within the multilateral framework for trade in services being negotiated, this would continue to frustrate the possibilities of developing countries benefiting from trade liberalization in services.

70 Findlay and Forsyth, *op. cit.*

71 *Ibid.*

72 Saurabh Srivastava, "Computer Software and Data Processing", in *Services and Development Potential: The Indian Context* (United Nations Publication, UNCTAD/ITP/22), p. 191.

Another question related to the cross-border movement of personnel concerns the recognition of professional qualifications. Many countries have instituted licensing procedures for the delivery of certain services which involves such movement. For example, foreign tour guides need to be licensed in many countries and are, in some cases, banned altogether.[73] Requirements regarding professional qualifications may function in certain cases as barriers to the delivery of services from developing countries. There is need for greater harmonization in this area as well, taking into account the specific requirements of the services.

Many Asia-Pacific countries are net-labour exporters. ASEAN as a group is a net-labour exporter as well, even though Singapore imports more work-force than it exports. These countries export a wide range of skills ranging from professionals to unskilled labour. The major destination of unskilled labour export from many of these countries used to be countries in the Middle East, but this pattern is changing. From ASEAN countries, there is greater migration to the newly industrializing and fast-developing countries in the region now.[74] Labour export is an important source of income for other Asian countries as well. In Sri Lanka, according to one study, it constitutes the largest component of service exports.[75] The movement of labour from many Asian countries to the Middle East is a case where labour has moved to capital and capital has moved to export promotion zones where cheap labour exists. For many Pacific Island countries, especially for the resource-poor countries, labour remittances are a major source of foreign exchange earnings. In addition to the export of unskilled labour to several countries, many of these countries also provide crews for shipping lines.[76]

A multilateral regime for increased international trade in services would need to address the question of cross-border mobility of unskilled labour. In services such as construction, the use of such labour is es-

73 Chow, *op. cit.*

74 Pang Eng Fong, and Linda Low, "Labour Mobility, Trade in Services and the Uruguay Round: The Perspective of ASEAN Countries", elsewhere in this volume.

75 R.A.M.C. Wanigaratne, "Services in the Economy of Sri Lanka", in UNCTAD, *Services and Development Potential, op. cit.*

76 Yee, *op. cit.*

sential for the delivery of the service. However, most developed countries have strongly resisted demands for increased labour mobility from developing countries on the grounds that this poses problems from the point of view of immigration. It is arguable that immigration rules tend to function here as barriers to a trade in services where many developing countries in Asia have a comparative advantage. In their proposals submitted to the Uruguay Round negotiations, developing countries have stressed that they are seeking more liberal provisions for the movement of personnel essential for the delivery of a service. There is no intention to meddle with immigration laws relating to citizenship and residence, but simply to ensure that immigration regulations dealing with temporary entry do not function as unnecessary barriers to trade in services.

Some of the countries in Asia and Pacific have policies and institutional frameworks for encouraging and regulating the export of labour, including a wider variety of occupations and skill levels. Thailand, India and the Philippines are examples of this.[77] It has been suggested that some of these countries might be in a position to export their skills in the management of labour export itself to other developing countries. It has also been noted by analysts that there is a need for more adequate institutional and regulatory mechanisms to facilitate increased labour flows between countries in the Asia-Pacific region. This would involve greater transparency and harmonization in immigration policies and in the mutual recognition of professional qualifications. At present, there is a provision for visa-free, short-term, non-employment related entry for ASEAN nationals in ASEAN countries, one result being an increase in intra-ASEAN tourism.

VI. GOVERNMENT POLICIES

In analysing strategies for enhancing the international competitiveness of developing-country service sectors, many authors emphasize the importance of government policies in realizing this objective. Indeed, the governments have the role of devising a strategy in consonance with the development needs and objectives of the coun-

77 Pang and Low, *op. cit.*

try in which the development of the service sector could play an integral part. In the context of the possibility of greater liberalization in international trade in services, governments would also need to ensure that such liberalization results in facilitating the realization of these objectives through technology transfer, employment creation, and better standards of living. They would also need to ensure that liberalization is carried out with adequate consideration to the asymmetries that exist in the international market and that it truly results in better opportunities of market access to developing country firms.

However, unless these strategies are formulated with adequate recognition of the changes in the nature of the service sector itself, and to the changes in the factors on which competitiveness is dependent, government policies can also act as barriers to the enhanced competitiveness of services. Many analysts point out the need for rethinking in the government policies in the service sector in order to take adequate account of these factors.

A number of import restrictions prevalent in several developing countries may disadvantage them in building up competitiveness in certain sectors. In Sri Lanka, the import duty on paper, instead of encouraging the growth of the domestic paper industry, seems to have had an adverse effect not only on the quality, range and efficiency of paper production in the country, but also on the printing and publishing services as well.[78] As a result, Sri Lanka has not yet been able to benefit from its comparative advantage in labour costs in building an export base for these services. Paradoxically, the import duties and restrictions have resulted in the situation where it is cheaper to print books abroad and import them back to the country. Noyelle points out a similar problem in relation to the policy of high tariffs on imported hardware as well as to that of domestic production of PC-clones.[79] This seems to have worked against sizeable economies of scale, especially since software is essentially a commodity business where achieving large scale is essential for bringing prices down.

78 Fernando, "Printing and Publishing in Sri Lanka", *Services in Asia and the Pacific*, Vol. 2, forthcoming.

79 Noyelle, *op. cit.*

Another government policy which might need some rethinking is in relation to certain sectors where State-owned enterprises seem to dominate the market. There are a number of sectors where the provision of services by the State has been seen as the only way to ensure their availability at reasonable costs to wider sections of the population. However, there are some sectors where the State-owned enterprises have branched into the commercial sector where they have an advantage over private firms on account of special privileges or subsidies. Banking in some Asia-Pacific countries is a case in point. There is a high degree of market concentration by State-owned banks in four ASEAN countries.[80] In some countries at least this has also resulted in problems of inefficiency and it has been suggested that an appropriate measure to stimulate greater efficiency might be a more liberal policy regarding the entry of new banks. However, this would need to be coupled with an adequate strengthening of the supervisory function of authorities and an improvement in prudential regulations. There are several instances in Asia-Pacific countries where there has been relaxation in State-ownership in order to open the financial sectors for competition. In many ASEAN countries, there has been deregulation of sectors such as banking. In the Republic of Korea, the reinsurance corporation founded by the government to strengthen the domestic capacity and to reduce the outflow of foreign currency, had the monopoly of both domestic and international reinsurance trade. The corporation was privatized in 1977, and there has been greater liberalization since then.[81]

Many analysts point out the prevalence of complex and not always transparent regulations and bureaucratic procedures as impeding the growth of service trade in several countries. In Sri Lanka, where the geographical position of the country can be effectively utilized to foster entrepot trading services, certain regulations and procedures seem to act as barriers. A greater harmonization of the various responsible organs of the government, such as the customs department, port authority, and the central bank, could facilitate the removal of some of these bottlenecks. The legal and financial requirements imposed by the govern-

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80 Mario Lamberte, "Trade in Banking Services: ASEAN Countries", elsewhere in this volume.

81 Park, *op. cit.*

ment for various stages of entrepot transactions also need to be relaxed for growth in this sector.[82] Similarly, the promotion of tourism calls for close co-ordination between various sectors such hotel, air transport, travel, etc. The absence of a supervisory body that can effectively unify the administrative and regulatory systems in the different sectors seem to hinder the growth of tourism and the ability to negotiate effectively with foreign suppliers in several countries.[83] In relation to labour mobility, analysts have noted the existence of complex and sometimes inconsistent rules and regulations in some Asia-Pacific countries, and the need for greater transparency therein.[84]

Many Asian countries follow specific policies geared towards the promotion of their service exports. Singapore, for example, has followed a highly focused policy since the early 1980s to transform the country into a computer-intensive economy.[85] This has involved the promotion of the use of information technology by all sectors of the economy, the development of strong hardware and software industries in the country, the spread of computer literacy across the labour force and the diffusion of information-technology applications within the public sector. Indian software firms are encouraged to export software by being allowed to import the necessary hardware free of tariffs, as long as the latter is used in a certain proportion in the production of exports. They can also benefit from relaxed foreign exchange rules. Recently, the Philippines has actively encouraged the build-up of a local data entry/processing industry through a number of measures including tax incentives.

In relation to the question of market access for service TNCs to developing countries, governments face almost opposing pressures from different segments of the domestic service industry. On the one hand, local firms that can take advantage of the presence of TNCs in terms of improved service inputs would as a rule favour liberalization of market access, and firms competing at a disadvantage in relation to the foreign firm might oppose this move. As Dorothy Riddle points out, "governments concerned with stimulating export earnings and generat-

82 Fernando, "Entrepot Trading Services", *op. cit.*

83 Chow, *op. cit.*

84 Pang Low, *op. cit.*

85 Noyelle, *op. cit.*

ing more jobs may find themselves torn between policy initiatives that ensure world-class business service inputs but little growth in export revenues or job creation, or initiatives that protect national firms at the expanse of the overall economic growth deriving from healthy export earnings."[86] Given the concentration of conglomerates in several service sectors, it is extremely difficult for small and medium-sized firms to maintain a client base. One way to encourage the growth of these firms is by requiring that certain business support services be contracted out to them by domestic and foreign conglomerates.

Furthermore, unless the domestic service sector has been trained to face competition, liberalization in international service trade can badly hurt the domestic firms in developing countries. This would appear to call for policies that encourage competition within the domestic service sectors, giving adequate incentives for investment, and creating opportunities for the development of private sector initiative. Proactive economic development policies - e.g. assistance in the purchase of external professional expertise, loan guarantees for successful service firms needing additional working capital but without hard assets to borrow, etc. - could play a positive role here. A rethinking of the tax structure, which was formulated in many countries in relation to manufacturing, is also needed in order to take account of the necessity of investment in telematic technologies.

Improvements in the telecommunication, transport and port facilities are indispensible for the growth of service exports. We have already noted some of the dilemmas that some developing countries face in reconciling overall development objectives and the requirements of promoting economic growth, in relation to the improvement of telecommunications facilities. In addition to these, the development of networking environments is becoming a priority in assisting domestic service firms to keep low costs and develop synergy with other firms.[87]

Studies have also noted the need for more focused export assistance programmes in identifying specific demands and specific markets. Information concerning international standards and quality control

86 Riddle, *op. cit.*

87 *Ibid.*

techniques would also need to be widely disseminated. Since the smaller domestic service firms in developing countries have few marketing resources, creating a "one-stop" service export support system might be very useful for providing market intelligence.[88]

Another aspect of developing-country efforts to promote their service exports is the importance of regional and sub-regional integration. Tourism is one of the sectors where there has been some progress in this direction among ASEAN countries. The provision of visa-free entry to ASEAN nationals for non-employment related purposes has assisted the growth of regional tourism in ASEAN.[89] Recently there have been efforts to offer joint tour packages involving several destinations in various ASEAN countries.[90] Here there can be a viable balancing of benefits through intersectoral exchange of benefits, as tourism involves several different sectors. Careful planning and coordination can produce competitive tour packages involving different countries in the region.

There are preferential regulations regarding the employment of ASEAN nationals in many of the member countries, in relation to the payment of deposits by employers. The embassies of some of the member countries in ASEAN capitals are also empowered to issue work permits. Greater clarity on immigration rules and greater harmonization of recognition of professional qualifications still need to emerge.[91]

A further area where regional integration efforts can lead to enhancement of service sectors could be in the field of financial services, where there might be opportunities for strengthening intra-ASEAN banking activities.[92] Recently there has been an agreement on using ASEAN currencies in intra-ASEAN trade. This could assist in the expansion of trade with ASEAN countries facing balance-of-payments problems or whose traders are covered by tight foreign exchange regulations. There is also the possibility of creating an interbank market

88 *Ibid.*, and Lamberte, *op. cit.*

89 Pang and Low, *op. cit.*

90 Chow, *op. cit.*

91 Pang and Low, *op. cit.*

92 Lamberte, *op. cit.*

among ASEAN countries, where some bankers are net lenders in the international market and some are net borrowers.

Regional integration in the European Community also presents problems for developing-country trading partners of the EC in some service sectors. One such area is civil aviation where it is feared that the proposed integration of the European civil aviation market will make it difficult for outside airlines to gain entry to intra-European routes and airport facilities.[93] One possible response to this situation from the developing countries might be regional integration efforts on their part - for example, ASEAN might gain from bargaining with the EC as one single unit.

Media services too can benefit from regional integration efforts. There have been attempts in this direction on the part of the European Community as well as among Latin American countries. The EC Convention on Transfrontier Television has come into effect. The Latin American Agreement on Cinematographic Integration made in October 1989 envisages greater collaboration among countries in the region in the production and distribution of films. In the Asia-Pacific region, based on historical association and cultural commonalities, it is possible to build a larger market for media products. Regulations that facilitate co-production and increased movement of personnel within the region can also result in access to technologies. Increased regional integration could also lead to harmonization in the updating of transmission technologies in the region and eventually to the creation of an Asia-Pacific Audiovisual Space.[94]

VII. CONCLUSIONS

The findings of these studies confirm that the developing countries, including those of the Asia-Pacific region have correctly identified their interests in the negotiation of the multilateral framework for trade in services. These positions have stressed the asymmetry which exists in the development and international competitiveness in services as be-

93 Findlay and Forsyth, *op. cit.*, and Boey, *op. cit.*

94 Vaidya, *op. cit.*

tween developed and developing countries, and the dominance of developed country firms in the world market for services. The studies highlight the importance of designing a multilateral framework for trade in services which foresees the need for measures by the developing countries themselves, and action by the developed parties to strengthen the domestic service sectors of the developing countries and provide them with effective access to world markets.

As has been illustrated with concrete examples throughout this volume, such measures include those of ensuring access to technology and training facilities, access to information networks and distribution channels, improved possibilities for the movement of labour at all skill levels and increased financial resources. It has also been demonstrated that it is essential that the mechanism devised for negotiating access to markets be such as to enable developing countries to impose commitments on foreign suppliers with respect to the above, and that such mechanisms permit the developing countries of the Asia and Pacific region to liberalize in those sectors or sub-sectors where such liberalization is judged most compatible with their development objectives, in return for meaningful access commitments by developed countries. It is also clear that effective international discipline of anti-competitive practices is essential in a variety of service sectors.

However, such a multilateral framework would only be effective in promoting these objectives if supported by determined action at the national level. The studies highlight the need for policies which take into account the various interrelationships between service sectors and between services and goods and the need for improvement in the basic infrastructures. Such policies should also aim at strengthening the competitiveness and efficiency of service sectors through providing increased competition at the national level, which will enable domestic firms to eventually compete with developed-country transnationals. Policies should be designed with a view to ensuring that domestic service suppliers are able to obtain maximum gain from the presence of foreign suppliers in the market, through the transfer of technology, training, access to their distribution channels and information networks, and by ensuring that they provide an effective market for local service suppliers, particularly small and medium-size enterprises. In many sectors vigilance is needed to ensure that anti-competitive practices do

not serve to discourage exports or artificially increase imports, nor enable foreign firms to "nip in the bud" the growth of independent competitive service enterprises in the region.

Co-operation at the regional and sub-regional levels is an essential tool for strengthening the international competitiveness of Asia and Pacific service producers - both intergovernmental, in order to overcome regulatory barriers to trade in services, and inter-firm, to establish regional and sub-regional alliances and networks able to compete effectively in regional and world markets. Such co-operation should be promoted at the national, sub-regional and regional levels and should be defended in multilateral negotiations.

PROFESSIONAL BUSINESS SERVICES IN ASEAN AND THE URUGUAY ROUND TRADE NEGOTIATIONS

*Sieh Lee Mei Ling**

INTRODUCTION

The inclusion of services in the Uruguay Round trade negotiations under the auspices of GATT has triggered off numerous issues that require close attention and consideration. Although broad macro-economic indicators of services development and trade are available in the ASEAN countries, a real understanding of the disaggregated sectoral positions necessary for meaningful negotiations remains alarmingly inadequate at a stage when signatories are almost at the point of committing themselves to the agreement. Given the limited time, it is not possible to compile and document detailed data at the industry level for the whole range of services, let alone perform an in-depth, systematic analysis of the implications for development and trade in each of them. This paper focuses only on professional business services. Three business services - namely market research, advertising, and accountancy - are selected for study in order to provide insights into some of the key issues that negotiators will have to consider while determining the appropriateness of positions for the development of their economies.

I. CONCEPTS AND APPROACH

Before proceeding further, it is necessary to define professional business services. The GATT secretariat proposed a list of nearly 40 diverse activities that may include numerous sub-activities. Thierry

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Noyelle has listed the following common characteristics shared by professional business services:

> professional business services are . . . services purchased primarily by other producers (i.e. by *firms*, not *individuals*) for the purpose of being consumed in further rounds of production. . . . are mostly in the business of delivering expertise, necessitating a major input from skilled or highly skilled professional, technical, and managerial personnel . . . comprise a mix of activities, some of which are restricted to licensed or accredited professionals, and others that are opend to all. . . . can be delivered either by firms, ranging from very large to very small, or by self-employed professionals . . . even in international markets.[1]

This paper specifically examines the following issues:

- Current market structure and domestic competition of professional business services; size of the market, concentration of suppliers and buyers, and recent trends that characterize local competition;

- Regional and international competitiveness when professional business services are traded beyond national boundaries; factors supporting trade and bases for competition within the sectors or industries, including the role of technology in enhancing competitiveness internationally;

- Barriers to trade in professional business services that arise from restrictive business practices and other corporate practices, regulatory, economic, technical, and professional considerations; and

- Possibilities of developing professional business service industries and increasing international competitiveness of their services output, including through the Uruguay Round trade negotiations on services.

The three specific business services chosen for analysis reflect various stages of development. Market research and market consultancy is a relatively young, small but rapidly growing business service. Up till the present, the industry has kept a low profile, enjoying

1 Thierry Noyelle, "Business Services and the Uruguay Round Negotiations on Trade in Services", in UNCTAD, *Trade in Services: Sectoral Issues* (United Nations Publication, UNCTAD/ITP/26), p. 310.

almost minimal interference in terms of regulations, and it harbours great potential for expansion. Advertising is by nature more conspicuous, often referred to in hefty monetary terms (when measured in billings), with established institutions either of the government or within the industry for self-regulation and accreditation. Many advertising firms are well-connected with internationally known names, and the sector is another candidate for future growth. Thirdly, accountancy and audit services is an older professional service industry that differs from the first two in that it is highly restricted to licensed professional individuals who adhere to regorous standards of practice. The profession has recently undergone changes due to technological improvements, such as computerization and service-product innovations. These changes stem from competitive forces and affects market structural forces.

The initial secondary data search on the three industries within ASEAN assisted more in planning the primary field work than in providing up-to-date, useable and comparable data. A nine-page question guide was prepared to facilitate in-depth discussion with leaders of the three professional business service industries in all the ASEAN countries, except Brunei (where these services are only beginning to develop). Face-to-face interviews were conducted with 35 individuals in April 1990 in the capital cities of the region.

The analysis is limited by the absence of reliable region-wide secondary data, the narrowness of scope of the services covered, the possible biases of prespectives from captains of the industries (though the interviewees have been carefully chosen in order to include views from local professionals in local firms or institutions, local professionals in foreign-linked firms, and a few expatriates). One major drawback concerns the fact that the views are verified only from other firms or professional bodies from inside the same industry, with the researcher as the sole independent ratifier. Sections II to IV present findings on professional business services based on the selected industries, corresponding to the first three objectives specified above. Section V discusses the possibilities of sectoral development and increasing international competitiveness through negotiations. Section VI concludes.

II. MARKET STRUCTURE, DOMESTIC COMPETITION AND RECENT TRENDS

This section briefly describes the basic structure of the three industries as the backdrop against which further discussion on trade and competitiveness can be conducted. In the context of developing economies, domestic market-structure issues - such as size, concentration and competition - may need closer examination than trade issues. Imbalances in development between segments of service-supplying firms make it necessary to give priority to an analysis of sectoral development rather than to a study of trade issues.

A. Market research

1. Size of industry and concentration

The market research industry in ASEAN is young (around 25 years old) and small in terms of dollar value of research service billing (only $34 million). The industry employs only about 1,400 permanent employees region-wide, with another 4,000 to 6,000 field workers employed either part-time or full-time. There are only 54 market research firms or establishments in the region and a few small operators who appear and disappear from time to time. In each country, the largest single company dominates about half the domestic market whilst the top five account for 90 per cent or more. Hence the extreme concentration of market power in a few large firms. This excludes some rather similar work conducted by general management firms, economic and business consultancy firms, and large accounting firms, often for government and semi-government bodies. A few large subsidaries of multinationals (e.g. Unilever, and Colgate Palmolive) and very large local firms (e.g. Keretek Cigarette and San Maru in Indonesia, Sihapart in Thailand) also have in-house research departments. In each country, they make up another $1.5 to 2 million, with somewhat more in the Philippine (see table 1).

In terms of services offered, even amongst firms within the industry, variation of service product mix is common. Generally, smaller

firms have a higher proportion of *ad hoc* than larger firms who tend to produce more 'packaged and branded' service output. As the industry expands, the market as a whole would see more of the latter and less of the former.

2. Foreign presence

In every country, market power is vested in foreign-controlled or managed firms, especially the two largest firms in each country, notwithstanding legal equity-ownership restrictions in Indonesia. Equity condition is one of the two important regulations in the industry, which has been operating in a relatively free environment. The other requirement concerns work permit requirements for expatriates. These will be discussed later in the paper.

3. Bases and intensity of domestic competition

Competition in the local market among large foreign-linked firms is based on expertise, knowledge and networking with research firms outside the country. Among the smaller firms, competition is determined by price, knowledge of culture and language ability. With growing domestic markets and almost the same number of firms, competition within each national market in the region is not very intense. This is particularly so when the industry is characterized by a small number of large firms oprating in a highly concentrated market. The relatively mild domestic competition is attributed to the increasing demand for market research services amongst the new generation of local managers (as in Thailand, Singapore and Malaysia) and greater awareness and use of such services amongst potential clients - even among those without a marketing background (especially in Indonesia).

4. Market restructuring

Over the past five years, the market has undergone restructuring at the international level, and this is reflected locally as well (e.g. AGB

bought into Survey Research Group whose subsidaries occupy the largest single position in every ASEAN country). Within each country minimal takeovers or mergers took place (e.g. Pulse merged with Unilever in the Philippines). However for the next five years, some international restructuring may occur when large research firms from the United States and United Kingdom (e.g. A C Nielsen, Burke, MBL or others) form tie-ups with existing firms. But new local entrants with regional association may emerge in the next few years (e.g. Inrasia). Evidently, in every country, firms with substantial foreign interests either directly or indirectly dominate the industry. Local firms lag far behind in size, market share, resource and technical capability.

B. Advertising

1. Size and concentration

There are about 540 registered advertising-agency establishments in the region, of which half are active, producing about $1.8 billion worth of billings and another half a billion dollars worth of non-media promotional activities. The regional market has been growing around 13 per cent per year in real terms on average, in the past three to five years. Employment is estimated to be about 13,000 persons in agencies excluding production houses and related industries. The largest single agency in each country commands slightly over 10 per cent of their respective national markets, whilst the top five account for an average of 34 per cent with the top 10 taking up about 58 per cent (see table 2). The industry in the region tends to see a proliferation of new, non-media services offered to clients. The larger agencies are increasingly competing on a range of peripheral services that include direct marketing, market research, market-strategy planning, public relations, non-media promotional activities, and other communication services. The share of above-line activities is naturally dampened although in absolute terms they have expanded considerably, if one judges from media expenditure. Small agencies tend to cater more to traditional media activities.

2. Foreign presence

Most of the larger agencies are foreign linked either through shareholding, management agreement, technical advisory agreement, referral agreement or simple association. At most, only two amongst the top agencies are owned and managed by nationals as majority of local agencies are medium to small in size.

3. Bases and intensity of domestic competition

Competition tends to be confined within market segments, though not totally compartmentalized. Local, small agencies tend to compete keenly for a limited segment of local advertisers and government accounts whilst foreign international agencies service large multinational clients and large local manufacturers. Foreign agencies offer benefits of networking in the region to clients requiring regional work, and compete on creative abilities, as well as on technical and financial capabilities. Local agencies offer personalized servicing to clients who need such services. They also offer lower prices through rebating or undercutting. Despite growing markets and the increasing use of advertising, especially by local clients, competition varies from strong (Philippines, Indonesia) to fierce (Singapore). Intensified competition in the region can be attributed to a number of factors such as:

- The entry of new locals into the market (Philippines, Malaysia) and arrival of new international agencies (Thailand, Singapore for regional market);
- Pressure from in-house agencies whose product managers want to place advertisement directly with media, bypassing agencies (Indonesia, Thailand); and
- Smallness of budget to yield sufficient commission in absolute amount, leading to competitive pressure arising from the cost angle. This happens especially when a lot of senior management input service is required, which can render operation expensive and complex.

4. Restructuring

A lot of restructuring took place in the last five years and more is expected in the near future. In general, restructuring was a result of market forces, because agencies - especially foreign - realigned themselves with others to follow clients. Several examples from advertising can be quoted where world-wide mergers are reflected in the region due to client-driven shifts in the global market. Some small, home-bred agencies have grown and are beginning to seek foreign partners to tap expertise, to forge international links and for financial resources. Also many new players are expected to emerge from foreign sources or even amongst nationals (Indonesia, Thailand).

C. Accounting

1. Size and concentration

The accounting profession, which is probably the oldest among the three industries studied, and certainly the most highly regulated both by the governments and professional institutions, is where information is most difficult to obtain. The size of the market in terms of billings for services is virtually not known to the firms themselves, not even to those who supervise their activities. This is due to the specific forms of business organization in the sector, i.e. partnership among the large and proprietorship among the small, rather than the corporate form where information would be more easily available.

The most reliable piece of information concerns the number of public accountants in the country. Altogether there are about 82,000 registered public accountants in the region of which 14,730 are in public practice (table 3). However, these figures are misleading because they are thrown out of proportion by the Philippine figures due to their large private-sector based education and training system. It is equally important to note that Indonesia is yet to legislate a law to exact compulsory auditing of company accounts by independent certified public accountants. Presently, government accountants in the tax department verify accounts only for purposes of tax collection, and this may explain

the large number of accountants in government service. The composition of registered public accountants by employment categories reflects regulations of admission into the profession. This further reflects the supply of accounting services and regulations on client firms and therefore the demand for services. The number of accounting firms is known in three of the five countries and the number of new entrants per year can only be estimated for Malaysia, Singapore and Thailand, as shown in table 3. The concentration of work in the few, large foreign-associated firms is probably the most pertinent characteristic of the sub-sector.

Larger firms have also enhanced their market positions by offering clients more than conventional auditing and tax services. They have definitely moved strongly into consultancy (both MIS and management), and into research. Small firms concentrate mainly on audit and tax work.

2. Foreign presence

Throughout the region, the dominance of the international Big Eight, now Big Six, is evident, despite the prohibition of foreign partners. Singapore is the only exception to this prohibition, and allows foreign partners so long as professional requirements are met. In other countries, foreigners not registered with recognized authorities are not allowed to perform audit work. They are permitted to function as technical advisers, MIS consultants and for non-audit work, subject to other immigration and work permit conditions. Nevertheless, international linkage is extremely crucial for referrals, technical assistance, training and other benefits such as image and reputation. Thus, it is not surprising that large, foreign affiliated firms account for well over half the market in each country.

3. Bases and intensity of domestic competition

Very little competition exists between local firms and foreign-related ones although competiton within segments - especially amongst

small local firms - can be intense. Large foreign firms tend to compete on their reputation, range of skill, services and knowledge, and their world-wide network, whilst small local firms compete on price, personalized service and relations with clients. But for the region as a whole, the demand for accounting services is increasing as a result of economic growth, and firms are expanding fast to cope. Professional bodies conducting training are also striving hard to increase the number of registered accountants and to upgrade standards and quality.

An exceptional factor that affected competition in the Philippines arose from changes in the political environment over the past five years. Some large firms had partners who moved into government and were able to expand quickly. Other firms have been able to take on the auditing of firms previously owned by people closely associated with the former regime and now temporarily managed by the government, pending enquiries on the involvement of public funds. Also, the Philippines Institute of Certified Public Accountants (PICPA), being a non-governmental organization (NGO), has been requested by the government to audit firms that no individual auditor would accept, PICPA acting as a middleman through which work has been channelled.

4. Restructuring

Restructuring amongst the large firms in the last five years were "imported" from international realignments due to client shifts. Medium-size firms are quite stable, but small firms tend to change partners frequently for business or market-share reasons, especially in order to meet the needs of growing clients.

D. Common features

A number of common features emerge from the above examination of the three professional business services in ASEAN:

- The sub-sectors or industries are not large but are experiencing very rapid growth in line with the general economic expansion in the region.

- The markets in the sub-sectors are highly concentrated in a few large service suppliers, whilst many small service firms - especially in advertising and accounting - share an insignificant share of the market.

- Within each industry or sub-sector, the service mix offered by firms need not be homogeneous, especially between size segments of service suppliers. The larger firms are innovative, moving into newer services for competitive and probably image reasons, whilst the smaller contend with the more traditional activities of their industry. Even among firms of almost similar size, heterogeneity of service products is not uncommon, probably as tacit complementation of one another and to avoid head-on collision in the larger segment. This could also be for finding the most competitive niche through specialization among smaller service firms, and to ward off forces of an intensely competitive environment.

- The sub-sectors have a strong foreign presence, either directly through equity and management or indirectly through technical agreements, referral arrangements or just in name (despite restrictions). Thus foreign providers of professional business services have already gained considerable market access and have established substantial presence in the region. As expected, foreign firms predominate as large suppliers at the upper end of the market.

- On the contrary, local suppliers of professional business services in ASEAN are confined to the lower end of the market, since they operate as very small-scale firms.

- Evidently, a dual-segment market structure is prevalent among the industries studied. Competition is segmented into two layers where large, foreign-linked firms service multinationals and large local firms by offering technological superiority, knowledge, and world-wide network and reputation. The small and medium local firms compete intensely for smaller clients who prefer lower price, personalized service, and knowledge of culture and language. The

fact that price can be depressed, especially in the small segment, indicates that competition in sub-sectors is not absent.

- Restructuring was rampant in the last five years, but most did not originate in the region. They were caused by world-wide realignment following client shifts. Amongst foreign-linked firms, restructuring was high in advertising and accounting, but less so for market research. Local medium-sized firms in advertising and market research look forward to having foreign partners for technical, financial and network benefits, but medium-sized accounting firms are generally stable. Small accounting firms, on the other hand, tend to change partners quite often to cope with growth in clientele. Such switches among service producing firms through mergers or acquisitions to consolidate or enhance market position suggest the prevalence of competition.

III. REGIONAL AND INTERNATIONAL COMPETITIVENESS

In view of the small volume of trade in professional business services conducted by countries in ASEAN, it is unrealistic to distinguish between regional trade conducted among ASEAN member countries, and international trade with other Asian countries and with the rest of the world. Given the level of development of the services, it is not surprising that whatever little trade that has taken place so far has mainly been confined to the region or at best with a few of the more developed Asian countries. Trade in services with the rest of the world hardly exists. Nevertheless, factors that motivate or impede trade tend to be similar for both regional and international transactions. They differ in degree rather than in kind.

A. Importance and factors for trade

Trade in market research, advertising and accountancy services are insignificant in terms of both exports and imports for each of the ASEAN countries. It appears that a slightly higher proportion of market-research services (about 20 per cent export and less than five per cent import) is traded than advertising services (10 per cent export and

less than that for import), probably due to the strong regional network of the two largest research firms. Cross-border accounting is negligible, if not almost non-existent, as national markets are virtually segregated by regulatory and professional barriers. The little trade that takes place in both market-research and advertising services can be attributed primarily to economic or business reasons, secondarily to geographical factors and then to cultural reasons in the case of market research and to technical factors in advertising. However, accounting services are traded predominantly due to technical needs (e.g. imports from United States), though geography may have some bearings (exort to neighbouring countries, e.g. attempts to export to Laos and Vietnam from Thailand and to China from Singapore).

B. Trading partners

ASEAN countries and other Asian countries (especially Japan and Hong Kong) appear to be the most important trading partners for market research and advertising. They are followed by the United States, United Kingdom, Western Europe and Australia. The high rank of ASEAN and Hong Kong is mainly due to regional networks for information exchange within the research firms and to the use of regional advertising material for advertising. Japan, United States and the United Kingdom are important foreign buyers of business services because of their need to market their products in the region (e.g. Japanese cars and other manufactured goods); whilst Australia and Hong Kong feature as important suppliers of commercial materials such as art work and technical assistance for video films and sound for advertising, and the United States for training and research.

C. Reasons for insignificant trade and competition

Regional and international trade and competition for professional business services in ASEAN are extremely limited, and confined to the larger, foreign-owned or affiliated firms providing market-research or advertising services. Small local firms are in no position to compete with them. Even among the large firms, the unimportance of regional and international competition is explained by at least three factors:

- The well-established intra-firm networks across countries automatically convert possible competition into complementary co-operation.

- Notwithstanding intra-firm connection, a research company (e.g. in Singapore) would commission work obtained in another market (e.g. Indonesia) to a local research company (in Indonesia), for the simple reason that it will not be possible to do the work themselves without local field-work support.

- Language, local knowledge and cultural differences inevitably reduce competition even within the territories of a country, let alone across borders, regionally and internationally.

However, in the regional market, competition does exist for government and internationally funded research (e.g. United Nations agencies). Another case is when management consultants who are not locally based enter the market informally. Similarly export or import of accounting services sometimes takes place for inter-agency requirements (e.g. a World Bank loan extended to the government may stipulate the use of consultants from outside the country as a condition).

D. Competitiveness and bases for regional and international competition

Large foreign-associated market-research, advertising and accounting firms consider themselves to be competitive in the regional market (even very competitive for market research), though only slightly competitive on a world-wide basis. From their own experience in the industry, human resources, knowledge, presence in a major market and financial capacity are regarded as very important or even critically important as bases for competition. Foreign-affiliated firms in the region appear to rate highly on these aspects. Substantial advantages appear to be obtainable through their wide networks which strengthen their ability to compete (e.g. financial back-up for bank guarantee in advertising, modelling techniques for market research from networks, ready support staff and facilities present in foreign markets). However, smaller local firms do not find themselves in the same league, as they are considered uncompetitive outside their national boundaries. Apart

from difficulties in matching the competitive advantages associated with large size, they lack adequately trained manpower, service-product innovation ability necessary for competition (probably due to weaker financial resources impeding investment in basic research technology), and a network of experts to draw upon.

E. Human resources

Human-resource problems that erode competitiveness appear in at least two forms in the region. In Indonesia and Thailand, they arise more from the insufficient number of adequately trained and highly skilled professionals (i.e. quality) whereas in Singapore and to some extent Malaysia, the problems take the form of sheer shortage of numbers (i.e. quantity). There, standards - even in small firms - are very high since they are manned by people who once worked with big firms and who are used to high standards of professionalism.

F. Financial resources

Financial requirements for competitiveness vary with the type of service activities (e.g. qualitative customized market research may require less sophisticated software and data-processing hardware as compared with quantitative "packaged" products conducted on a large scale). They also depend on the system of operation within the country. For example, advertising agencies in Singapore and Malaysia require substantially more financial support in order to obtain bank guarantees equivalent to the credit value granted by media owners in comparison with Thailand, Philippines and Indonesia where no such requirements exist.

G. Quality of location

The location of a service industry can sometimes seriously affect its regional and international competitiveness and its ability to win contracts. Some important factors that determine the quality of location of professional service firms include the ability of the respective governments to provide:

- Adequate communication facilities (liberal in Singapore and Malaysia, poor in Thailand, the Philippines and Indonesia);

- Up-to-date and reliable statistics for a good sampling frame for market research (good in Malaysia and Singapore, poor in the Philippines, Thailand and Indonesia);

- Adequate educational system and training facilities for human-resources development (good in Singapore and Malaysia for accounting, weak in Indonesia);

- Efficient administration with minimal bureaucratic delays, e.g. to enable fast turnaround time, especially in dealing with trade in advertising, as in Singapore; and

- Technical availability and advancement, through work-permits issued to foreign experts for creativity, media capability and support work when needed in advertising (good in Singapore and Malaysia, but restricted in Thailand, Indonesia and the Philippines).

H. Technology and competition

In view of the emphasis placed on human resources, expertise and knowledge for the competitiveness of professional business services, let us examine the technology issues that are important for competitiveness. What are the local technology inputs critical for competitiveness of local service firms in the region? What are the foreign technology inputs critical for their competitiveness? What are the main factors that affect access to and mastery of such foreign technology? What are the main forms of technology transfer from foreign to local firms? What are the main challenges and opportunities in taking advantage of critical technologies to improve competitiveness?

Apart from knowledge of local culture, language and business practices, there is virtually no other local technology input that is important for competitiveness. It is evident that the region relies heavily on foreign sources of technology for professional business services. This includes market-research techniques (latest market-modelling techniques); software for specialist know-how such as television audience

measurement and for advertising pre-test; creative techniques for commercials (computer animation, montaging); skills of account planning for effectiveness of MIS computer consultancy (in banks or for telecommunication) for accounting firms. Such ability to access technology from overseas depends on several factors, the most important of which is whether a firm is locked into an international network or not, irrespective of the manner of linkage. Such association may be in the form of equity participation by foreign shareholders or partners, management agreements, licencing agreements, other technical arrangements or through loose, informal relationships. Tapping into a network for technology and assistance is often a privilege accorded to associates, rather than just based on costs. Secondly, training effected either directly through training programmes or by staff exchange - internationally or intra-firm - is vital for professionals in order to keep abreast of technological developments. Training by foreign experts brought in from affiliates is certainly an effective mode of technology transfer in all the three industries considered. Thirdly, availability of finance has been cited as a determinant for access to technology that requires investment in capital equipment or royalty payment (especially for market research).

There are several opportunities for the region to increase its competitiveness by taking advantage of the possibilities provided by technological advancement. These include the rapid development of infrastructure in the region in order to permit the use of some of the computer-based technologies, growing awareness of the benefits of computerization, and the more wide-spread adoption of new technology which in turn drives business firms to upgrade themselves to meet clients′ needs adequately. However, the region also faces several challenges in using technology to improve its competitiveness. Readiness of professionals to accept such new technologies in terms of availability of skilled manpower is indeed not widely prevalent, given the absence of adequate financial, technical and professional resources. Although they account for a very small proportion of services produced by value, they constitute the bulk of the number of service-supply firms. This implies that priority should focus on their development needs rather than on their immediate ability to trade. In the long term, uplifting them and preparing them for international competitiveness, though

hypothetical, would be a useful approach in planning programmes for their improvement and development.

Secondly, foreign trade and competition are confined to a small number of larger, usually foreign-related service firms, that produce the bulk of the work. Even then, the proportion of service output that is traded is insignificant, not exceeding 10 per cent either way on average. The only important exception is found in the advertising industry of Singapore which acts as a regional centre, where about half the service output is intended for outside. To a smaller extent, one of the large market-research firms with a regional office in Kuala Lumpur also imports and re-exports services for their network. Generally, accounting firms do not perceive any relevant degree of competition. Market-research firms describe competition in their sector as insignificant within the frame of a network. Advertising agencies who cater to the region consider competition as keen in Singapore and, to a smaller extent, Malaysia, but agencies from other countries would regard such competition unimportant. As for regional competitiveness, the general preference of consumers in favour of large firms has been cited as a concern by all the three industries in each country.

I. Summary

It is difficult to distinguish between regional trade (within ASEAN) and international trade (other Asian countries and rest of the world) because the differences appear to be those of degree rather than of kind. Moreover, given the extremely limited experience in international trade and the small volume of regional trade, attention tends to revert to raising the currently low level of development of the industries as a precondition for trade.

The level of regional and international competitiveness of ASEAN professional services, judged by the three industries, must be analysed against the duality of their domestic market structures. With the markets segmented into two distinct categories of service suppliers in terms of size and foreign linkage, which in turn determine their capabilities and competitiveness, general statements on competitiveness within the region or internationally must be made with caution.

The nature and intensity of competition faced by local firms that are generally small is vastly different from what is observed in the large foreign-dominated segment. Firstly, local service firms rarely think in terms of markets outside their country. Many firms, especially in accounting, do not even think beyond the town where they are located. They have difficulties in preventing clients from moving to larger service firms when their businesses grow, after initial efforts in getting clients to use their services. Possibilities of export are very high for market research and strong for advertising and accounting, while international competitiveness are rated slightly lower. Human resources, knowledge, networking ability and finance have been considered as very important bases for competitiveness beyond the national boundary. Although in terms of technical competence and knowledge, the large advertising and accounting firms consider themselves to be as competitive as firms in other countries and those in market research very competitive, reservations have been expressed concerning the shortage of qualified highly-skilled manpower in the region (Singapore and Malaysia for specialist advertising skills, e.g. copywriting, media planning; Thailand and Indonesia for advertising and accounting, e.g. computerized MIS).

International tie-ups, regardless of form, have been emphasized as important for competitiveness because they are crucial avenues for accessing up-to-date technologies (e.g. computer graphic design for advertising, specialist software for market research, latest practice methods and standards for accounting). Foreign parent firms or affiliates not only supply trainers and technical expertise but also financial support (especially for advertising agencies in Malaysia and Singapore whose media owners require collateral backed bank guarantees) and client referrals including global contracts obtained by parent firms (e.g. McCann for the world-wide Coca-Cola account).

Whilst linkage with international firms increase competitiveness, participation in a network tends to decrease the need to compete, because a substantial volume of trade actually occurs intra-firm, hence resulting in a reduction in real international competition. Further, arguments for assistance from government or elsewhere, towards export development or import restriction seem to be weakened by the fact that benefits of support programmes would be shared with foreign interests. This necessitates further understanding on various foreign affiliations

that range from equity ownership through technical agreements to mere use of a foreign name. Such an analysis is beyond the scope of this paper.

Moreover, the degree of international competitiveness must take into cognizance the service product mix offered by the industry within the country. Even among the top firms within a particular service industry, the lines of businesses or services offered by one firm are often different from that of another firm, in which case they do not compete directly with each other. For example, HRM, the largest local Malaysian accounting firm, merged with Arthur Andersen recently due to the fact that their business strengths complemented each other, the former being strong in auditing and tax but weak in consultancy, and the reverse being true for the latter. Thus, market concentration may be less than what is made apparent by the number of firms and business volume. It may be more accurate though difficult to go by the broad category of services offered rather than by conventional industry or subsectoral type classifications. By this approach, *ad hoc* customized market-research consultancy can be added to similar work performed by advertising agencies and by general management consultancy firms. Similarly, media research and public relations work in market-research firms can be added to similar work in advertising agencies (and to specialist public relations firms) in order to determine market concentration of service activities.

IV. BARRIERS TO TRADE

An examination of the regulatory and professional institutions of the three professional business services reveals at least five broad categories of delimiting factors for trade such as border difficulties, professional qualifications, technical constraints, economic hindrances, and corporate practices. Though in practice the issues overlap or converage, they are discussed separately for clarity of exposition.

A. Border difficulties

A major characteristic of services trade, as distinct from trade in goods, is the frequent need to involve the movement of factors or production, particularly service-providing people, across countries (e.g.

MIS consultants would find it impossible to advise clients from a distance). However, the bureaucratic difficulties in obtaining work permits and in complying with immigration rules in the region are well known. Except in Singapore, work permits are issued only to a small few - such as for training and consultancy in accounting firms, and for technical expertise and training in advertising agencies and market research. The need to develop indigenous expertise is probably a stronger justification used by governments than simple employment creation.

Secondly, difficulties are also prevalent in trading services embodied in goods. Malaysia severely disallows totally foreign commercial talent or material in advertising as a means to protect her infant advertising industry. Similarly, Indonesia bans all foreign-printed material whilst Thailand permits up to 20 per cent of foreign content.

Thirdly, a strong deterrant to market access in establishing a long-term presence is effected through equity-ownership rules in all ASEAN countries except Singapore. Since the 1970s all service businesses in Indonesia are 100 per cent locally owned. In Thailand, foreigners are limited to 49 per cent equity except for firms established before the Alien Business and Occupancy Law of the early 1970s (e.g. Lintas is owned 80 per cent by United Kingdom interests), and old United States firms under the United States Parity Rule can still be 100 per cent owned (e.g. O & M). In the Philippines, the 1986 Constitution limits foreign equity to only 30 per cent by 1991, except for the United States firms established under the United States Parity Rule. Malaysia and Singapore do not restrict foreign entry and establishment but Malaysia encourages at least 30 per cent Bumiputra (indigenous) participation and preferably 51 per cent Malaysian equity, especially to bid for government work. However, throughout the region, technical and advisory agreements with foreigners are permitted, though subject to visas and work permits for entry.

Another form of difficulty for service import are the duties and taxes payable at the border. For example, Malaysia levies a withholding tax on imported market-research data or for services performed by a non-resident, even when they are intended for re-export. This discourages trade as it pushes up cost. Dispite general economic prosperity in the region, foreign exchange regulation associated with shortage of for-

eign exchange to pay import bills remains a trade barrier, especially in the Philippines. Government procurement rules that usually favour small, local service firms (e.g. advertising in Singapore, accounting in the Philippines) or follow national socio-political objectives (e.g. the New Economic Policy conditions in Malaysia) constitute an obstacle to large foreign service suppliers.

Language requirements for supplying services (e.g. training manuals and delivery in the local or official national language), though not insurmoutable, tend to keep out imports. Regionally, English is commonly understood and used by professionals and large business. This has resulted in a lowering of such barriers for trade within the region and with English speaking suppliers.

B. Professional qualifications

It is necessary to distinguish between professional services that can be performed by individuals who are required to meet conditions of training and examinations in order to be registered for licence by the government and/or recognized professional bodies (as in accounting) and those that are open (as in market research and advertising). Focusing on the former, conditions regulating registration and practice concern initial admission into the profession and the renewal of licence to continue. In ASEAN, governments play a major role in such regulations (e.g. the Minister of Finance in Indonesia, the Malaysian Institute of Accountants which is a statutory body under the Ministry of Finance, the Board of Accountancy under the Professional Regulation Committee of the Philippines, the Public Accountants Board of Singapore, the Board of Supervision of Accounting Practice of the Ministry of Commerce in Thailand). Apart from academic qualifications, the criteria for initial registration may include the length of practical experience, nationality (Thailand), residency (Singapore), age (Singapore), membership of a professional institute who oversees standards and ethics, good character, and proficiency in relevant local laws pertaining to the corporate sector and tax in general. Hence suggestions to establish equality in professional qualifications for "entry" recognition and to harmonize standards of practice in order to facilitate trade in such services will be far from easy. This does not include further requirements for periodic renewal of professional practising licence

- such as continuous professional education - which are compulsory in some countries (e.g. the Philippines) - but voluntary though encouraged in others (e.g. Malaysia, Singapore and Thailand).

C. Technical constraints

The most formidable technical barrier to services exports from ASEAN is their relative technological backwardness in relation to world standards. The dynamic innovations in technology vastly affect the production and delivery of professional business services to the extent that the level of sophistication or lack of it greatly determines their competitiveness and ability to trade.

Secondly, the rapid computerization of crucial stages of service production and the use of information technology can also in effect function as technical barriers to trade. Trading partners often need similar technological levels and similar infrastructures to deal with transactions within firms. For example, hardware and software compatibility is a technical precondition for trade in market research. These preconditions here take the form of computer programmes and of telematic facilities in trading countries.

Readiness and ability of human resources with appropriate skills need to be ensured in both the exporting and importing countries in order not to hinder trade. In particular, the exporter would need to train the importer and to assist in the installation and use of specific technology after the transaction is effected (e.g. software for specialist market-research jobs).

D. Economic hindrances

On the supply side, the smallness of the domestic market inhibits service producers to attain a 'critical mass' that is necessary for scale and scope economies before stepping outside national boundaries into foreign markets (e.g. advertising in Indonesia). This implies that opportunities for service firms to move down the learning curve are restricted by the size of the domestic market, whilst cost efficiency will not be reachable within the context of a small market. Cost competitiveness is difficult to attain when the domestic market base is small because it

does not provide sufficient work volume for sharing fixed costs of service businesses. Moreover, the lack of intense competition in the domestic market need not be a favourable sign for export capability because industries need to sharpen their efficiency through the process of strong competition. Thus the domestic market structure itself constitutes a formidable trade barrier.

This situation is aggravated by the low absolute value of net revenue obtainable from a small domestic market which will not yield attractive margins for enterpreneurship and will not encourage entry into service business. An example of the former is seen in the small commission derived from media expenditure in Indonesia. The absence of local entrepreneurial activity in Singapore advertising has been cited as an example of the latter. Thus, the problems of smallness of service producing units or firms, particularly among the medium and small segment, seem to perpetuate a vicious circle in ASEAN, hence limiting their ability to improve on cost efficiency and competitiveness to be able to export.

Increasing labour and overhead costs in the more export-oriented countries (e.g. Singapore) is also eroding the competitiveness of their professional service business. Rising costs constitute barriers to their export.

The strength of the Singapore dollar vis-à-vis weaker currencies in the region and elsewhere has also made export expensive. As in the case of goods, currency differentials which at times drive trade may also hinder trade.

ASEAN professional business services would be crippled without foreign technological, financial and management support. Without efforts to develop indigenous resources, export capability would be severely hampered.

On the demand side, clientele in the region for imports appears small because export of professional business services is dependent to a large extent on goods export, especially of national brands. Service exports seem to be restricted since they tend to follow the export of goods, and since there are not very many ASEAN brands that are exported.

E. Corporate practices

Several points raised earlier in this report are in fact barriers to trade that originate from corporate behaviour. Increasing intra-firm transactions effectively means market sharing on a regional or international basis to the detriment of real free trade. Potential ASEAN services exporters would prefer to let their world-wide networks handle international demand. Technical agreements and arrangements pertaining to management, licensing, training, referrals, etc. amount to intervention on market forces and to the discouragement of trade. Even the association of independent market-research firms through Inrasia, a company formed in Hong Kong to foster international linkage amongst regional firms, disrupts free trade by creating intra-group trade. Mergers and takeovers world-wide, commonly seen amongst large advertising and accounting firms and also amongst some small local accounting firms, have also reduced competitive forces, apart from introducing or causing instability in the market.

Supply-driven hindrances are also common. The rapid diversification of services within international firms means the creation of large multiactivity service producers who concentrate market power not only domestically but also on the trade front. This includes the large variety of peripheral services offered by advertising agencies in their efforts to create one-stop communication centres (e.g. research, market consultancy, public relations, direct selling and client promotion below the line), as well as management-consultancy services provided by accounting firms for non-traditional areas such as manufacturing integrated system.

The business behaviour of service firms also tend to perpetuate the dual-segmented market structure, which is not conducive for trade promotion for the country as a whole. With a dichotomized market where little linkage exists between the two segments, opportunities for growth and development of service firms, especially from the small segment, would be hampered. Such growth is vital as a precondition for trade. Hence, intentionally as well as indirectly, the corporate behaviour of service firms may have contributed towards the erection of another trade barrier.

V. DEVELOPING PROFESSIONAL BUSINESS SERVICE INDUSTRIES AND INCREASING INTERNATIONAL COMPETITIVENESS

In the Ministerial Declaration launching the Uruguay Round, it was specified that trade expasion was intended to serve as a means to economic growth and development. Measures to increase trade, such as liberalization or transparency, are expected to contribute to development through trade. This approach involves offering quality services at competitive prices through cost economies of efficient industries that can meet the needs of international markets competitively. The negotiations on trade in services is mandated to respect the policy objectives of national laws and regulations applying to services. It is no secret that many of such policies pursue economic and social development as prime objectives, whilst trade expansion is relegated to a lower step in the process. Initial import-substitution policies that precede export-oriented ones give priority to development rather than to trade, at least in time.

Given the present level of development of professional business services in the ASEAN region, it is slightly premature to address issues raised by and agreed upon within the Group of Negotiations on Services in Montreal at a sectoral or subsectoral level. The region has very little services trade experience to draw upon, Singapore being the only exception to this. The new challenge of having to assess possible gains from freer trade (and investment) in specific services and to protect national interests through concessions obtainable is indeed formidable.

In order to safeguard their interests, it is important that ASEAN countries, along with other developing countries, need to be part of any rule-making process on international services trade. It is also prudent to be involved in a multilateral framework than in bilateral agreements. Having established a regional mechanism, ASEAN may attempt to harmonize their positions and compare notes internally, particularly at the subsectoral or industry level, in order to enhance the opportunity of their being heard and bargaining strength.

Nevertheless, developing countries of ASEAN should show their commitment in working towards a global system for orderly trade in

services in two ways. First, general principles for the promotion of free trade, and for justice and equity should be agreed upon within the context of a multilateral framework for the benefit of all trading partners. Secondly, ASEAN countries should contribute to the agreement by indicating service sectors, subsectors or activities, where they are ready to permit foreign access, at least initially. Simultaneously, ASEAN countries should explicitly state what they expect of trading partners and potential partners, especially from developed countries. This includes symmetrical treatment of labour of all skill types and levels, concessions for development purposes, flexibility in the use of government subsidies and assistance for export promotion, time allowance for implementing concessions, flexibility to change regulations and laws to accomodate future development needs, provisions that take into account weaknesses arising from balance-of-payments and debt positions, and remedial action necessary to make up for the general technological and capital deficiencies of developing countries. Detailed requests would need to be made for all services or for specific service activities. Considerable understanding needs to be obtained on such specific questions, after reaching an initial agreement on the principles of the trade framework.

Each of the substantive issues raised for negotiation on trade in services is discussed below with reference to market research, advertising and accounting in the region. They are approached by evaluating possible contributions toward the growth of ASEAN subsectors and hence towards economic development and trade.

A. Mobility of factors of production

The single most important and beneficial outcome, expected of the agreement on services at the subsectoral level, is the possibility of improving technology through greater inflow of foreign experts. Without exception, all three industries in all ASEAN countries favour relaxation of immigration and work-permit rules to fulfil their dire shortage of highly skilled, up-to-date experts, especially in order to train locals. It is recognized that controls on specific time period, professional qualifications (specific job and purpose of entry for short term relocation of professionals who need a presence in the client country), would be necessary for security reasons and for regulating skill devel-

opment and employment opportunities for locals. Except for Singapore, which is already very liberal, others in the region are awaiting such mobility to boost subsectoral development and competitiveness.

Singapore even hopes to see the arrival of a greater numbers of unskilled or semi-skilled workers to alleviate its labour shortage,[2] whilst the Philippines is keen to export labour-intensive work through freer labour movement into foreign markets, for foreign-exchange gain (e.g. for market-research data processing services). However, without a symmetry clause to permit the inward mobility of skilled professionals and the outward mobility of unskilled labour through recognized organizations, such an aspiration of developing countries may be construed to be against the principle of reciprocity - another area for negotiation.

Nevertheless, the relatively more advanced subsectors in ASEAN such as advertising in Singapore and accounting in Malaysia may be able to increase export of their services with easier mobility of professionals, notwithstanding other licensing conditions, particularly for accounting. A quota system has been suggested for regulating the number of foreign licensed professionals admitted to work to facilitate trade, where quotas may be determined by the level of economic development.[3]

B. Market access

At the industry level, none of the three professional business services studied consider foreign competition to be threatening, since the largest international firms are "already here". They are firmly established and are practising successfully (e.g. the Big Six in accounting; top advertising agencies such as Saatchi & Saatchi, McCann Erikson, Lintas, BBDO, J. Walter Thompson, Ogilvy & Mather, Foote Conne & Belding; and AGB in the Survey Research Group for market research). Singapore even argued that more international firms located in the country would enable further export of services and contribute

2 Sieh Lee Mei Ling, "Malaysian Workers in Singapore", *Singapore Economic Review*, April 1988, pp. 101-11.

3 J. Barton, "Negotiation Patterns for Liberalizing International Trade in Professional Services", *University of Chicago Legal Forum*, Vol. 1986.

to alleviating some limitations of smallness of their domestic market. The Philippines considers international firms as channels through which their abundant skilled manpower could be mobilized for accounting and advertising and for labour-intensive work such as data entry for market research. The presence of foreign service firms would serve as a link to export markets.

However, it is realized that foreign establishments exist under rather stringent equity conditions, professional licensing controls and restrictive government procurement policies, which together serve as a protective umbrella for the local firms. It is felt that direct presence such as through uncontrolled equity participation should not replace the present arrangements of limited ownership or of correspondent, referrals, technical and management agreements. This is mainly in order to prevent unfair economic competition and to promote the development of local firms. The dominance of foreign service suppliers would stifle the ability of locals to start (e.g. worry of absence of local entrepreneurship in advertising in Singapore, hence a barrier to entry) and to grow (e.g. generally all three industries see difficulty in expanding their business without associating themselves with foreign firms). With competition already biased towards internationally connected firms who are more capital and technology-intensive, the fear that local firms will be adversely affected by liberalization cannot be ignored.

Consideration would need to be given to studying the proliferation of contractual arrangements that are likely to emerge as trade in services becomes increasingly liberalized, if developing-country interests are to be protected. New forms of co-operation that facilitate trade and at the same time ensure social and economic development should be specified and encouraged. Conditions such as local-employment stipulations, minimum training requirements by budget allocation, investment in equipment relevant for production or delivery of services, linkage with small firms and earmarking a portion of the business for export could be considered in this respect.

C. National treatment

The national treatment principle can be supported on at least two grounds in ASEAN. First, in order to foster intra-regional trade and

subsequent world-wide trade, the countries that are more prepared for this should not be obstructed by trade barriers within the region, given the already small quantum of trade presently seen (e.g. Singapore's regional role for advertising production has been reduced becuase of local content rules in neighbouring countries). Secondly, for pure cross-border transaction of services, often embodied in goods, barriers should be dismantled (e.g. a 15 per cent withholding tax is levied by the Malaysian Government on the imported market-research materials and on payments to foreign service suppliers). Perhaps more conditions can be placed on trade that requires movement or entry of service suppliers into the country for safeguarding jobs as well as national interests.

Although foreign firms are generally well-treated in ASEAN, the issue of national treatment seems to appear in three forms. Firstly, problems stemming from professional qualifications, licensing and standards of practice can be difficult to resolve, even within the region (especially for accounting practice, as well as advertising ethics and prohibitions). Perhaps efforts in equalizing qualifications for entry and on harmonizing standards of practice should be initiated within the region as a first step, in order to promote development and trade. Secondly, incompatibilities and lack of understanding of cultural and social value systems, including language, can prove to be an obstacle to national treatment. For example, advertising in Indonesia and business practices in general would necessitate cognizance of their "rukun" concept of peaceful co-existence. In Malaysia, ethnic and religious sensitivities may hinder full participation of foreigners. Thirdly, associated with development objectives, countries in ASEAN would have to balance not only foreign and local interests, but also the interests of sub-groups within the country which often involve a complex of factors originating from ethnic, religious, geographical, income and occupational differences.

D. Reciprocity

Though acceptable in principle, developing countries - including the ASEAN countries - would face difficulties in putting this concept into practice in relation to the import and export of services, including those requiring the mobility of factors of production. On the export side, experiences from both the Philippines and Thailand with the

United States Parity Rule - in effect a reciprocity rule - cast doubts on its helpfulness in practice. The principe is useful only if technical and economic development levels are similar or if they can be matched.

Regarding import, there is a strong need to protect local firms on a low level of development from unfair competition. They need to be allowed enough time to catch up on basic skills and technology. Further, national redistribution policies geared towards overall economic and social development are also necessary.

E. Transparency

The formal requirements, if agreeable, to furnish relevant rules and regulations on licensing conditions and to notify technical, health or safety standards should not pose difficulties, even though this may require time. But problems may be arise with respect to gathering such information from institutions within the public and private sectors initially. However, the growing level of professional awareness and exchange will increasingly facilitate the disclosure of clear, unambiguous technical standards. But as with other developing countries, ASEAN may need to ask for flexibility in the introduction of changes in rules and standards, which may be necessary frequently to keep pace with the development process. It may not be feasible to open the content of the rules or changes to consultation without hampering the growth process.

However, developing countries may benefit from some agreement on dispute settlement procedures in order to resolve differences concerning policies as well as implementation. It is premature to anticipate the precise form such procedures may take. Formal agreements would need to replace informal and unwritten rules and business methods in many countries, and this may not prove to be easy. Complex bureaucratic procedures would need to be simplified as well.

F. Progressive liberalization

For countries whose service industries are ready to trade, either purely across border or through short-term relocation of professionals, or even to establish a temporary commercial presence in the importing country (such as Singapore and to a lesser extent Malaysia) liberali-

zation of foreign markets are crucial both for business expansion and for creating a regional network.

Even for the rest of ASEAN who may be able to export services to lesser developed countries before too long, any agreement on liberalization will help. However, presently ASEAN tends to be more an importer, especially when trade in services entails the presence of service firms and inbound service providers. In either case, concensus on measures for gauging the level of competitiveness at domestic, regional or international levels should be reached. Even if there are agreed measures, the issue of the extent of market opening has to be discussed. In goods trade, the graduation of countries has usually been determined on the basis of per capita income or economic growth. However, as mentioned above, the heterogeneity of services activities within subsectors need to be taken into account in assessing the ability of countries to compete. It is difficult to see how such disaggregated considerations can be incorporated in the negotiations.

G. Interests of developing countries

We have already examined many of the major issues that pertain to the development dimension of trade in professional services. Many countries regulate domestic business conduct and transactions in this sector for a variety of reasons. For example, apart from reasons of sovereignty, national security and national integration, media-related industries like advertising are regulated in relation to language use, standards of practice and explicit value preferences.

Indonesia disallows TV commercials on State channels because of the possible negative effects of consumerism among the masses. They also disallow professional testimonies and political insinuations in advertising. In Malaysia, disruptive foreign influence on local religious beliefs and values are prohibited whilst interracial harmony promotion is encouraged. Political opinion polls as a research activity is virtually banned in Indonesia, Singapore and Malaysia. As political stability is crucial for attracting foreign investment as well as for economic prosperity in general, there are regulations on a number of diverse activities including traded services.

Apart from health and safety standards, professional qualifications sometimes stipulate the exclusion of non-nationals (e.g. accounting in Thailand). Attempts should be made to ensure uniformity within the region in order to facilitate intraregional trade and to form a common front in international trade negotiations. However, efforts by national governments to control the process of development according to their individual economic development strategies should be respected.

Clearly, to promote subsectoral development, professional business services in ASEAN need more training, technical assistance, foreign networking, more market knowledge of potential clients, more practice in the domestic competitive environment (e.g. introducing anti-trust laws) and also government initiatives (either as subsidies, tax incentives or control). In the context of the Uruguay Round negotiations on trade in services, the governments are expected to balance the expected gains from trade expansion on the one hand and the protection of national development goals on the other. To achieve that, more in-depth analysis of the services sector and subsectors should be pursued.[4] More intra-regional exchange and co-operation should be mobilized in order to enhance bargaining strength vis-à-vis potential trading partners, primarily from developed countries. Further alternative approaches for exchange of concessions should be explored both during the negotiations as well as after the initial agreement is reached.[5]

VI. CONCLUSION

There is a great need for developing countries to accord high priority to the development of their service sector, including professional business services, which have remained fairly insignificant in their trade until now. It is imperative that developing countries involved in

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4 Sieh Lee Mei Ling, "Services in Malaysia: Microeconomic Issues for Research" in Sieh Lee Mei Ling ed., *Services in Development: An Agenda for Research in ASEAN*, Manuscript Report 198e (Ottawa, International Development Research Centre, 1988), pp. 201-24.

5 See G.C. Hufbauer, and J.J. Schott, *Trading for Growth: The Next Round of Trade Negotiations* (Washington, D.C., Institute for International Economics, 1985); and J. Mark and G.K. Helleiner, *Trade in Services: The Negotiating Concerns of the Developing Countries* (Ottawa, The North-South Institute, 1988).

the negotiations concentrate on how to garner benefits from the participation and presence of foreign service providers, for the development needs of their countries, including the development of indigeneous or local enterprise and expertise within those service industries, in a manner acceptable to both foreigners and locals. This necessitates control of foreign involvement such as through reasonable conditions for market access on the one hand, and strict disciplines for local service industries who will be beneficiaries of promotional incentives on the other.

Box 1

PROFESSIONAL SERVICES IN THE URUGUAY ROUND CONTEXT

Efforts to liberalize trade in professional services in the Uruguay Round context have had to differentiate between those services where no accreditation or licensing is required, the main barriers here being those related to the entry of persons concerned to foreign markets (e.g. visas and work permits), and those where even if the person is allowed to enter the market, he/she cannot provide the services without receiving a license or accreditation from a government or private body. Market entry is also restricted by the dominance of large transnational firms in certain sectors. [a] The Group on Professional Services has focused on the following issues: (i) the definition of professional services, the categorization of professional services into accredited and non-accredited, the difference of scope of professions in different countries and their heterogeneity, the specific categories of personnel who are allowed temporary entry, and the need to have an illustrative reference list of accredited and non-accredited professional services; (ii) the applicability of principles and concepts such as national treatment, non-discrimination, market access, MFN, increasing participation of developing countries, and the mechanics of exchange of concessions in this sector; (iii) accreditation, harmonization, mutual-recognition agreement, national and sub-national regulations, and public or private regulations; (iv) the application of different modes of delivery - namely, cross-border movement of professional services, temporary presence and right of establishment (entry and operation conditions) and the importance of transfer of payments; (v) the difference between services rendered by individuals and those rendered by firms; and (vi) the need for an annex or sectoral annotation.

Many special characteristics of interest in the professional services were highlighted in the Group as follows: (i) the professional services consisted of a wide range of heterogeneous services; (ii) some professional services were licensed or accredited by governments or by private professional bodies to maintain standards; (iii) there were differences in the scope of professions in different countries and there were differences between countries in requiring accreditation/licensing in a given profession; (iv) some professional services could be delivered across the border by telecommunications, while others required temporary presence and some others required establishment of firms; (v) some professional services were performed by individuals acting on their own account and others were delivered by firms or groups of professionals; (vi) regulations were developed by governments at the national or subnational level or by professional bodies; (vii) barriers exist in both accredited and non-accredited services, including denial or selective issuance of visas and work permits, regulatory impediments to commercial presence, subsidies and government aid, problems of access to services, and maintenance of recognition of qualifications; (viii) role of mutual-recognition agreements and their relationship to the framework; and (ix) applicability of the formula approach to this sector, in particular to the non-accredited professional services.

The need to examine whether and how the framework would result in the liberalization of certain aspects of professional services was stressed in the Group. These included the cases of non-accreditation, non-recognition of foreign qualifications, non-recognition of non-citizens or non-residents, requirements of joint venture or prohibition against joint venture, restriction of staff that could be employed, prohibition of using firm's name, denial of access to transborder data flows or telecommunication services, and denial of taking examinations for completion of qualifications.

Most countries believed that an annex would not be needed and supported a horizontal approach to this sector. The United States, on the other hand, submitted two annexes to the Group - on accountancy services and legal services. The Group, in its last meeting in October, decided that this sector did not require an annex but that certain specificities of this sector required additional provisions in the framework. There was also a general agreement that coverage should encompass as many professional services which are internationally traded as possible and that this sector should include both delivery by individuals and firms. Special

Box 1 (Continued)

PROFESSIONAL SERVICES IN THE URUGUAY ROUND CONTEXT

attention should be given to agreement on mutual recognition of qualifications and to developing objective criteria for establishing minimum standards or harmonization of standards.

Special attention was given to transparency requirements (both as regards what countries required and how these requirements were to be met), given the requirements for prior approval of professional qualifications and licensing, notification of appropriate regulatory bodies, and examination procedures to facilitate work on harmonization and mutual recognition. Developing countries pointed out that prior to the negotiation of mutual-recognition agreements, parties of the framework should be notified so that they could fully participate in the formulation of standards. Transparency was also found relevant in cases of regulations imposed by private professional associations and, as self-regulatory bodies were fully independent, the question was raised on how they could be made to comply with the requirements of the framework. It was pointed out that governments should ensure that the relevant private associations would abide by the rules of the framework. The United States found that transparency procedures were needed, including a contact point which would provide information on who regulated, what the regulations were, what the means of qualification for non-nationals or non-residents were and whether there was a need for review/appeal procedures in cases of refusal.

The need for prudential regulations was highlighted, and it was pointed out that liberalization should not lead to dilution of standards. Japan expressed concern that the existence of differences in the qualification and certification systems were prohibitive of trade in services in the accredited areas and referred to the need for the application of national treatment and harmonization. The recognition of qualifications was of utmost importance as the key to market access, and relevant domestic regulations and standards should be based on objective criteria. The fact that mutual-recognition agreements would be open for accession for all parties is not by itself sufficient, as all parties should also participate in the negotiation and formulation of standards. If stringent developed-country standards were applied in mutual recognition, developing-country service suppliers might be excluded from trading in certain sectors.

Developing countries were also concerned about the conditions for temporary mobility of labour as visa problems can restrict their ability to trade both accredited and non-accredited services. This issue has been addressed in a proposal regarding "Temporary Movement of Service Personnel" submitted to the Working Group on Labour Mobility, which would allow the temporary movement of all categories of service personnel essential to the effective delivery of a service covered by the framework agreement. It would also ensure that immigration regulations neither act as an unnecessary barrier to trade in services, nor nullify and impair the benefits expected under the framework. [b] Developing countries have stressed the need for access to professional service markets, information, technology and distribution networks, financial support and training, as well as preferential agreements between developing countries.

The difficulty in strictly applying the MFN principle in the absence of internationally accepted minimum standards or mutual recognition of qualifications has been emphasized by the United States. However, other countries have supported the full and unconditional application of MFN to trade in professional services from the outset of the agreement; the related issues of standards, technical qualifications and mutual recognition should not necessarily be seen as an MFN question, but rather as an aspect of domestic regulation.

The importance of the positive list approach was stressed by developing countries. Different modalities for negotiating market access were discussed, such as bilateral request/offer negotiations and formula approach where certain kinds of activities would be liberalized by all participants in a uniform way and to a uniform extent. The United States has referred to the

Box 1 (Continued)

PROFESSIONAL SERVICES IN THE URUGUAY ROUND CONTEXT

need to draw up a list of professionals to whom entry could be granted immediately through simplified immigration rules, recognizing that entry alone did not give the right to practice. It was also pointed out that the non-accredited professional services could be candidates for early liberalization by the formula approach, i.e. that a set of conditions would be agreed upon and applied to an initial list of professional services.

a Thierry Noyelle, "Business Services and the Uruguay Round Negotiations on Trade in Services", *Trade in Services: Sectoral Issues* (United Nations Publication, UNCTAD/ITP/26), pp. 309-63.

b See discussions in the context of labour mobility elsewhere in this volume.

Box 2

ILLUSTRATIVE LIST OF ACCREDITED AND NON-ACCREDITED PROFESSIONAL SERVICES

This indicative list of accredited and non-accredited professional services has been used as a reference in the discussions in the Working Group on Professional Services in the Uruguay Round.

A. Activities generally considered to be accredited professional services:

- Legal professions (lawyers, solicitors, etc.)
- Legal advice/consultancy
- Accountancy services (accounting, auditing, taxation advice, insolvency)
- Architectural services
- Construction and engineering services
- Quantity surveyors
- Health services (e.g. medical and veterinary practitioners, nurses, pharmacists, dentists, opticians)
- Linguistic services (e.g. interpreters)
- Others (e.g. estate agents, patent agents, actuaries, notaries, stockbrokers, teachers, psychologists, tourist guides, criminologists, journalists)

B. Activities generally considered not to require accreditation and often referred to as business services:

Marketing services

- Advertising, direct marketing and sales promotion
- Market research and public opinion polling
- Public relations
- Fairs and exhibitions, other marketing services

Consultancy services

- Management and administrative services
- Computer related services and software development
- Recruitment consultancy
- Training and education services/consultancy
- Other specialisations (e.g. mining/geology, agriculture and fisheries)

Box 2 (Continued)

ILLUSTRATIVE LIST OF ACCREDITED AND NON-ACCREDITED PROFESSIONAL SERVICES

Operational services

- Provision of personnel (e.g. secretarial, temporary labour)
- Contract cleaning services
- Waste disposal and processing
- Security services
- Translation services
- Other operational services

Other technical services

- Maintenance and repair of equipment
- Quality control and inspection
- Testing and certification
- Design
- Photographic services, commercial art
- Other technical services

Other business services

Table 1

THE MARKET RESEARCH INDUSTRY/SUBSECTOR IN ASEAN 1990

Country	No. of Firms		Estimated size of industry (non-market research) million dollars	Estimated Employment	Growth (per cent)	Market concentration (per cent) Top 1	Top 5
Indonesia	10	3.5	(1.3)	210	na	50	85 [a]
Malaysia	10	9	(1.5)	350	na	50	95
Philippines	20	7.3	(20.0)	400	na	45	90
Singapore	5	7.8	(7.8)	200	40	40	93
Thailand	9	6	(1.5)	250	25	50	90 [b]
Total	54	33.6	(32.1)	1,410			

a Top 3.
b Top 2.

Table 2

THE ACCOUNTING INDUSTRY/SUBSECTOR IN ASEAN 1990

Country	No. of firms	Estimated size of industry	No. of public accountants (practising members)	Estimated employment	Growth of new public accountants (per cent per year)	Market concentration (per cent) Top 6
Indonesia	264	unknown	8,000 (800)	unknown	unknown	65
Malaysia	625	unknown	5,500 (1,650)	19,000	3.6	unknown
Philippines	unknown	unknown	60,000 (10,000)	unknown	unknown	75
Singapore	280	unknown	5,000 (530)	10,000	12	unknown
Thailand	unknown	unknown	3,500 (1,750)	unknown	5.7	unknown
Total			82,000 (14,730)			

Table 3

THE ADVERTISING INDUSTRY/SUBSECTOR IN ASEAN 1990

Country	No. of firms (active)	Estimated size of industry (below the line) billion dollars	Estimated Employment	Estimated real Average annual Growth (per cent)	Market Concentration (%) Top 5	Top 10
Indonesia	75 (35)	280 (280)	2,800	14	35	55
Malaysia	75 (38)	280 (0.5)	1,200	20	50	70
Philippines	153 (59)	211 (100)	2,599	20	43	70
Singapore	88 (50)	660 (100)	3,000	14	18	60
Thailand	150 (88)	398	3,500	23	23	34
Total	541 (270)	1,829 (480.5)	13,000			

COMPUTER SOFTWARE AND COMPUTER SERVICES IN FIVE ASIAN COUNTRIES

*Thierry Noyelle**

Computers are at the core of a formidable technological revolution. This revolution is transforming radically the way in which outputs - manufactured, service, and even agricultural outputs - are produced in both developed and developing nations.[1]

To be sure, this is not the first time that a major technological innovation has resulted in a fundamental upheaval in how societies produce. However, unlike earlier technological revolutions of comparable magnitude - such as the invention of the steam engine or that of the discovery of electricity - the diffusion of computer technology necessitates not simply the introduction of a new class of machinery (computers) but also, and at least as importantly, the development of a new range of services (software).

In 1989, expenditures for computer hardware and peripherals, computer software, and related computer services in all market economies was estimated at about $600 to $700 billion, a value equal to or larger than the GNP of most developing and developed countries. Of this sum, between $250 and $300 billion was spent on computer software and computer services, including software and services produced in-house by computer users themselves (internal expenditure) and those purchased on the open market (external expenditure). The estimate for 1989 is that approximately $120 billion, or from 40 to 45 per cent of the

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1 This paper is based predominantly on interviews conducted in five Asian countries between May 1989 and March 1990 with senior managers and adminstrators working for key software firms, equipment manufacturers, industry publications, industry associations, and government agencies. While the paper reflects my views, I am most grateful for the tremendous assistance and generosity I received from everyone during my visits to Asia. Without such help this study would not have been possible.

total computer software and computer service expenditure, was spent on the open market.[2]

Data collected by the OECD suggest that in 1987 the United States market alone accounted for perhaps as much as 50 per cent of total external expenditures for computer software and services, followed by Western Europe with a 25 per cent share, Japan with an 8 to 9 per cent share, and all other market economies accounting for the remaining share.[3]

Data presented below suggest that the five Asian developing countries analysed in this report - India, Singapore, the Philippines, Hong Kong, and the Republic of Korea - spent perhaps as much as $2 billion on computer software and computer services in 1989 (internal and external expenditures combined). Together, the computer software and computer service industries in the five countries created jobs for perhaps as few as 70,000 or as many as 90,000 computer operators and professionals, programmers, systems analysts, designers and engineers.

While some of these numbers may seem small when compared to corresponding numbers for developed countries, they are not negligible when related to the gross national product or to the employment base of the five countries.[4] Computer software and computer service jobs are often among the highest paying positions in the five countries. For example, compared with the Filipino average annual income of about $1,700, a Manila programmer with three to four years of experience might have earned as much as $2,500 plus bonuses in 1989.[5] Hong Kong senior computer professionals are paid nearly as much as in the United States (an annual average of $65,000 including bonuses for someone with 10 to 15 years of experience), far more than the average for many other occupations in the Territory. In addition, the computer software and computer services industries are sectors that experienced

2 These estimates are based on *The Internationalization of Software and Computer services*, Information Computer Communications Policy, Study No. 17 (Paris, OECD, 1989). See especially table 2 and annex tables 1-35.

3 *The Internationalization of Software and Computer Services, op. cit.* See especially table 2.

4 The United States, for example, was estimated to have over 2.5 million jobs in computer software and computer-related occupations in 1989.

5 John Maxwell Hamilton, "A Bit Player Buys into the Computer Age", *The New York Times Magazine*, The Business World, 3 December 1989.

very fast rates of growth in the five countries during the late 1980s (25 per cent or more annual rates of growth during those years were not uncommon) and whose rapid development is as critical to the transformation of these economies as it is to that of more advanced countries.

This paper describes and analyses the development and internationalization of the computer software and computer service industry in India, Singapore, the Philippines, Hong Kong, and the Republic of Korea. Its objective is to review recent and current developments in the industry in the five countries and draw lessons that can help shape an Uruguay Round agreement on trade in services that can best assist the development of the domestic and export capacities of developing countries in this critical area of the services.

This paper comprises seven major sections. Section I describes the structure of today's computer software and computer service industry. Section II calls attention to the importance of internationalization in the industry and describes the industry's principal modes of delivery. Section III presents the state of development of the industry in each of the five countries. Section IV examines barriers to trade confronted by the computer software and computer service firms from the five countries. Section V discusses the competitive weaknesses and competitive advantages of computer software and computer service firms from the five countries in both domestic and foreign markets. Section VI reviews the range of measures taken by the five countries to strengthen their domestic and export capacities as well as additional measures that they might take within or without a multilateral agreement on services to strengthen such capacity. Particular attention is given to the issue of how best to promote the development and transfer of computer software and computer service know-how.

An important finding of this research, and one that it is useful to stress at the very outset, is that in an industry traditionally viewed as being dominated by firms from developed countries, three of the five countries examined here have succeeded in developing a strong export capacity - namely India, the Philippines, and Singapore - in the areas of contract programming (India and the Philippines) and packaged software (Singapore). In addition, the fact that Hong Kong and Korea

have not developed a similar export capacity does not necessarily reflect poorly on the local software industry. Rather it is the reflection of acute shortages of personnel in the face of very rapidly rising local demand for computer software and computer services. Indeed, at least in the case of Korea, there is every reason to believe that, once the current manpower shortages have lessened, local entrepreneurs will be able to develop a vigorous export capacity, especially in the area of packaged software. In sum, this study suggests that even in this area of highly skilled services, certain developing countries are coming to the negotiating table with strong assets in hand.

I. THE STRUCTURE OF THE COMPUTER SOFTWARE AND COMPUTER SERVICE INDUSTRY

The roots of an independent computer software industry go back, in part, to 1969 when IBM, under antitrust pressure, was forced to unbundle (i.e. to price separately) its software products from its hardware products as part of a consent agreement with the United States Justice Department. Until the late 1960s, hardware manufacturers followed IBM's lead and typically sold operating software and some applications software bundled with their hardware, making users responsible for developing other applications. Large firms wanting to take advantage of the new technology on their own would set up systems divisions to develop and operate applications on their own computers; firms lacking resources or firms choosing not to develop an in-house computing capability could hire data processing bureaux to develop and run applications on their behalf.

IBM's unbundling of its software products facilitated the emergence of an independent software industry. In addition, the falling prices of computers and the introduction of minicomputers in the mid-1970s greatly increased the number of users, including many who were willing to own and operate their own computers but who preferred to rely on vendors for applications. Together, these developments contributed to the formation of a market for software products, both custom-built and "packaged" (standard) software.

The independent market for computer software and computer services that has developed is a complex and highly segmented one that

involves a range of actors and numerous market niches based on both the type and the complexity of the service rendered. A minimum understanding of these layers of segmentation is necessary in comprehending the challenges, difficulties, and opportunities encountered by firms in different segments of the industry.

A. Wide range of providers

Today's market for computer software and computer services is served by a range of providers including not only independent software houses and service bureaux but also hardware manufacturers and hardware distributors who may also sell software developed by themselves or by others. In addition, large users also may retail to outside users applications developed originally for the firm's own use. For example, a number of large banks from advanced economies sell data processing and software services to other banks.

This diversity of supply is reflected in Datamation's annual rankings of the world's 25 largest software producers and 25 largest suppliers of computer services (including data processing, systems integration, and facilities management) shown in Tables 1 and 2 repectively. When looking at Tables 1 and 2, the reader should note the formidable presence of IBM in software, a presence which is six times larger than that of its nearest rival, Fujitsu. The reader also should note that these lists are quite consistent with the pattern of regional market shares described earlier: 30 of Datamation's top 50 firms are United States firms, 13 are Western European, and seven are Japanese.

B. Broad mix of services

A second order of industry segmentation is that based on the type of service provided. From the viewpoint of users, providers of computer software and computer services can now offer a variety of services at both the developmental and the operational stages.

1. Developmental stage

At the developmental stage, users may choose from among a variety of options ranging from one extreme - complete out-sourcing of the development of a new system - to the other extreme - total in-house development. In so doing, they have recourse to the following range of services:

(i) Systems integration

With this option, the user contracts with specialized vendors to develop a complete system, including purchasing the necessary hardware and assembling the needed applications software, which can include a mix of packaged and custom-built software. Systems integration is also referred to as "turnkey system" development, although the latter term is often used more narrowly to refer to the development of custom-built software only. Note also that originally systems integrators did not engage in the development of custom-built software and confined themselves to the use of packaged software. Increasingly, however, they do so or at least customize available packaged software to meet specific client needs. Large systems integrators include such firms as EDS (a subsidiary of General Motors), TRW, Digital Equipment, Andersen Consulting, IBM, Cap Gemini Sogeti, Martin Marietta, and Ernst & Young.

(ii) Packaged software

The user may choose to assemble a new system by purchasing new hardware or using an old one, and buying a standard or "packaged" software. Today, there are thousands of software packages sold to run applications as diverse as payroll, personnel, inventory control, accounting, word processing, computer-aided design (CAD), computer-aided engineering (CAE), and many others, especially in the area of general business applications.

In the personal computer (PC) market, packaged applications are the dominant form of software. This is not the case in the mainframe or minicomputer market, although the share of packaged software in both markets increased sharply during the 1980s, especially in the United States and Western Europe. The Japanese have been slower in adopting packaged applications, owing in part to a tendency among Japanese commercial computer users to think that their needs are unique and can only be met through customized applications. This is changing rapidly, however, since the desire for custom-built applications is running against limitations in local software production capacity arising from serious shortages in software personnel and a huge backlog of orders for applications. In addition, the Japanese are beginning to realize that their emphasis on custom-built applications is often unwarranted and, for that matter, a rather unproductive way of achieving quick diffusion of computerized technologies. Among the top providers of packaged software are most computer manufacturers such as IBM, Fujitsu, NEC, UNISYS, and Digital Equipment, as well as large independent houses such as Computer Associates, Oracle, and Dun & Bradstreet software subsidiaries for mainframe and minicomputer software, and Microsoft, Lotus, and Novell for PC software.

(iii) Custom-built software

If packaged software is not available to meet their needs, users may turn to an independent developer to custom build software. While this may require the software developer to write, line by line, a completely new programme, increasingly software houses are developing customized software applications either by piecing together standard modules from their own proprietary software library or by modifying standard, packaged software. This trend towards using versatile, modular software in order to custom build software is likely to accelerate in the years to come as the a result of a conceptual shift in the way in which applications software is developed, namely through the introduction of "object-oriented" software design. In object-oriented software design, large software applications are written as a set of

interlocking, yet fully self-enclosed, modules that can be modified or replaced as needed.[6]

Nearly every major computer manufacturer develops custom-built software, as do a number of systems integrators and some independent packaged software houses. More importantly, this is a field in which thousands of medium-sized and small firms operate along side independent programmers and the systems divisions of users.

(iv) Systems consultancy

Users may limit their reliance on outside expertise to systems consultancy including advice on purchase of hardware and software or advice on the best way to use a particular packaged software. For example, they may need advice on how to use a packaged data base software to set up a computerized client file. Large accounting firms are major players in systems consultancy, especially in the area of systems design.

(v) Contract programming

The user may choose to develop his/her own software, but may need additional personnel at the developmental stage. The user can then turn to an independent software house which may either dispatch analysts and programmers to the client's site or be hired as a subcontractor to develop parts of the client's project. The use of subcontracting and personnel dispatching, also called "body-shopping", is widespread throughout the industry not only between software houses and final users but also among software houses themselves. This is because in an industry in which individual firms are subject to variations in personnel needs, linked to abrupt changes in the number and size of projects, body-shopping is a way in which individual firms can adjust to temporary surges or troughs in staff needs as new projects begin or old ones end. As indicated later in this report, not only is the use of

6 Andrew Pollack, "The Move to Modular Software", *The New York Times*, 23 April 1990, pp. C1-C4.

body-shopping and subcontracting widespread in the domestic software industry in almost every country, increasingly the practice involves cross-national relationships, including a number of firms from the five countries studied here.

(vi) Training and education services

Finally, regardless of the extent to which the user chooses to externalize or internalize the development of a new system, the user may call upon the services of a specialized trainer to assist in the preparation of personnel who are either in charge of developing the new system or who are targeted to use it.

2. Operational stage

As is the case at the developmental stage, users also have a variety of options to choose from in running their computer applications at the operational stage.

(i) Service bureaux

As in the past, users may continue to use the services of data processing bureaux, although this practice is less common than it once used to be. The major firms in the industry are EDS and ADP.

(ii) Facility management

Short of contracting out all of their data processing work to a service bureax, users may turn over the management of data-processing facilities to a service firm. Under this option, users retain ownership of the facility. EDS, ADP, Andersen Consulting, and a few others are prominent in this field.

(iii) Software maintenance and systems conversion

During the life cycle of a system, users may call upon the service of a vendor to maintain their software. The service may include assistance in implementing upgrades of operating or applications software, debugging existing software (no software is ever error free), as well as software conversion. As hardware manufacturers introduce new computers with brand new operating software or with more advanced versions of existing operating software, or as users altogether change computer suppliers, users may need to upgrade their applications software in order to "migrate" from one operating environment to another. To do so, users may contract with an independent software house to adapt the old applications to the new computing environment. Typically, the original developer of the software is involved in its maintenance or conversion.

(iv) Data-entry encoding

In preparing data-processing jobs that demand large amounts of encoding, users may call upon the service of a data-entry firm to carry out the task on a contractual basis. As I shall indicate in this paper, this is one area, although in no way the only one, in which several developing countries have attempted to build an export business.

C. Segmentation by degree of complexity

Last, but not least, the degree of product complexity is an important dimension of segmentation in the industry. A traditional distinction is that between systems software and applications software. Users need both kinds of software to operate their computers.

Systems software is software that instructs the computer on how to process and store data, or on how to move data from one part of the computer (e.g. the central processing unit or CPU) to another (e.g. a disk drive where data are typically stored). This class of software includes:

- Operating software, which runs the basic computer unit and is developed typically by manufacturers (e.g. MVS which runs IBM

mainframes, VAX which runs mini and supermini computers manufactured by DEC, MS-DOS which runs IBM PCs and IBM PC-compatibles);

- Data base management systems (DBMS) and relational data base management systems (RDBMS) software which is used in the management of large computer networks (United States-based software houses Computer Associates and Oracle are dominant players in this domain at the moment);

- Utilities software, including add-ons to basic operating software to run special peripheral equipment as well as communications software; and

- Programming languages.

Applications software is designed to solve particular business or engineering problems. There are many kinds of applications software, owing to the great diversity of uses to which computers are put: word processing, accounting, payroll, spreadsheets, computer-aided design (CAD), computer-aided engineering (CAE), computer-aided manufacturing (CAM), computer-aided software engineering (CASE) tools, artificial intelligence (AI) applications, etc.

Typically, systems software - and more particularly, operating software - is seen as the most demanding area of software work as measured by human resource inputs. This is because of the complexity of the algorithmic mathematics involved in developing such software and the need to assemble large pools of systems analysts and designers trained in these complex areas of mathematics. This is an area which is dominated by hardware manufacturers, a few specialized software houses, and a few highly sophisticated users. For the moment, this field of software development remains largely out of reach of the software firms and users from developing nations, if only because they lack trained personnel.

Within the area of applications software, there is also a gradation in the level of difficulty involved in software development, linked to the degree of complexity of the application itself. General business software (word processing, spreadsheet, accounting, payroll, client file systems)

is usually viewed as relatively easy to develop; CAD/CAE/CAM software, CASE tools, and AI applications are viewed as much more difficult to develop.

II. INTERNATIONALIZATION AND MODES OF DELIVERY

With the exception of the United States market, nearly every domestic market for computer software and computer services in both the developed and the developing worlds depend heavily on imports or on the local sales of affiliates of foreign firms, mostly from the United States. This is in part a result of the unique historical role played by United States firms in the development of the industry.

As a group, United States firms dominate the world market. The often used estimate is that the United States market represents approximately half of the world market (in terms of external expenditures for computer software and computer services), but that United States firms capture nearly 70 per cent of world sales. This gives United States firms a whopping 40 per cent market share outside the United States.[7] This is achieved through direct exports from the United States as well as through local sales by the foreign affiliates of United States software suppliers. The United States does import computer software and computer services, but these imports are small relative to the size of the United States domestic market.

In contrast then, almost every other market depends heavily on either or both imports or local sales of foreign affiliates of mostly United States firms. This dependance is overwhelming in the area of operating software. Only since the introduction of PCs and engineering work stations has the United States dominance in the area of operating software begun to be challenged. But dependence on United States software is also strong in the area of application software, simply because the development of the United States market is so much more advanced than it is elsewhere.

7 United States Congress, Office of Technology Assessment, *International Competition in Services* (Washington, D.C., U.S. Government Printing Office, 1987), Chapter 5.

Of course, not all application software is suitable for import. Simple applications such as payroll or personnel files tend to be highly country-specific since they must be designed to satisfy tax and other statutory reporting requirements dictated by local law. Word processing must be designed to handle the local language. These and other applications are among the kinds of software products that are routinely produced locally. For example, a firm like Citicorp - probably one of the world's most sophisticated commercial users of computer systems with a highly developed in-house software development capacity - will routinely purchase and utilize locally developed personnel and payroll applications software.

The fact that most countries depend heavily on United States software does not mean that most run a trade deficit in the area of software, although probably many do. For one thing, as discussed below, the potential for "pure" cross-border trade in software remains limited and dependence on United States software products often takes the form of programmes or services that are produced locally by affiliates of United States firms and that thus do not affect directly the balance of payments. In addition, a number of countries do seem to be able to balance their direct imports through exports of their own, if not even generate a surplus. As was noted in the Introduction, this is indeed what appears to be the case in three of the five countries studied here, with India and the Philippines generating a software trade surplus, and with Singapore most likely being able to balance its software imports by strong exports.

In theory at least, computer software and data processing firms can trade their services through three principal modes:

- "Pure" cross-border trade;
- The movement of the consumer to the location of the provider; and
- The movement of factors of production (labour, capital, and technology) to the location of the consumer.

"Pure" cross-border trade in computer software and computer services means the provision of a service, without the movement of ci-

ther consumers or producers, and implies a transfer of information between producers and consumers in the form of a business letter, a business report, a telephone conversation, a computer-to-computer transfer of electronic information via telecommunications, the exchange of electronic files stored on material support (disk, tapes, etc.) via the mail, and other similar means.

The usual argument is that the intangible nature of most services makes pure cross-border trade very difficult to achieve but for a few service sectors. In this respect, however, computer software and computer services often are singled out as among the few services for which pure trade is possible because of the availability of various communications media appropriate to their transfer. Several firms, for example, reported working on software conversion projects using local IBM terminals connected continuously on-line with the mainframe computers of their overseas clients. In practice, though, even in the case of software packages, remote data entry, remote data processing, or remote programming, the extent of pure cross-border trade in computer software and computer services remains limited for the reasons explained below.

To serve foreign markets, producers of software packages must have access to a local network of distributors. While such networks exist in most countries, very few include truly independent distributors. Most software around the world remains distributed either by manufacturers or by large independent software firms. Both manufacturers and independents rarely have the long-term interest of a third-party product at heart but instead tend to give preference to their own products or to fast selling packages, quickly abandoning one third-party package for another if sales decline. Consequently, in order to penetrate foreign markets, producers of software packages often find it necessary to establish their own commercial sales presence. In addition, the installation of a complex applications software package often requires initial assistance from the provider and access by technical personnel to the client's site. After-sales services by the software developer may also necessitate the presence of a locally based hot-line technical staff as well as on-site assistance from trainers.

Likewise, even in the data processing market, firms trying to serve foreign markets will often find it necessary to establish a minimum sales presence to sell products locally.

In most other areas of the industry, such as custom-built software or systems integration, pure cross-border trade is usually not a substitute for other modes of trade but rather occurs in conjunction with the other two modes of trade. This is because much of the production process in these areas remains embedded in a direct relationship between client and producer. For example, systems analysts, systems designers, and project managers who produce custom-built applications must spend many hours on client premises, identifying, analyzing, and designing systems. In turn, programmers must work under the supervision of project managers, wherever they are located, and in some cases, may need to work directly on the client's computer. The same holds true for systems integrators, whose primary services include systems analysis and systems engineering.

Within the context described so far, it is no surprise to find that United States software suppliers play a significant role in nearly all of the five markets studied in this paper and that the form of their presence varies significantly depending on the type of service rendered. What is more surprising, however, is to find that exports of computer software and computer services are significant for several of the countries studied. In much of the remainder of this paper I try to explain how these and other significant developments have come about and what are their implications for the current multilateral negotiations. First, I review the state of the market in each of the five countries.

III. COMPUTER SOFTWARE AND COMPUTER SERVICES IN THE FIVE COUNTRIES

Table 3 summarizes market conditions for computer software and computer services in the five countries in 1989. The measures presented in Table 3 are based on extremely limited data available from the five countries, and must be regarded with some caution. Despite these limitations, I estimate that the total market size (total internal and external domestic expenditures plus export sales) for the five countries

reached approximately $2.2 billion in 1989. Of this amount, domestic plus export sales amounted to nearly $1 billion, or approximately 45 per cent of the total market. Total exports from the five countries for the same year stood somewhere between $140 and $170 million, originating overwhelmingly from India, Singapore, and the Philippines.

On the import side, rough estimation would show total direct imports by the five countries in 1989, ranging anywhere between $95 and $190 million - from 15 to perhaps as high as 30 per cent of all sales in the five countries' external domestic markets. In addition, sales by local affiliates of foreign firms (including fully owned affiliates, joint ventures, and foreign-linked partnerships) might be estimated for the same year at perhaps as much as 20 per cent of all domestic sales, depending on the country (see the last column in Table 3). In sum, through both imports and sales by local affiliates, foreign firms in 1989 might have controlled anywhere between 25 and 50 per cent of total sales in the external domestic market of the five countries. However, when related to total domestic sales (external and internal expenditures) the market share of foreign-linked firms was obviously much lower since in-house production (internal expenditures) by users - overwhelmingly domestic firms - continues to account for more than half of the market in each of the five countries.

Finally, as it has been noted already, the rough aggregate balance between direct imports and direct exports in and out of the five countries reflects different trends on a country-by-country basis. In this respect, the measures presented in Table 3 suggest software trade surpluses in the case of India and the Philippines, a balanced account in the case of Singapore, and software trade deficits in the case of Hong Kong and Korea.

A. India

In 1988-1989, the size of the Indian external computer software and service market was estimated at between Rs 2.5 and Rs 3.0 billion ($250 to $300 million), roughly two-thirds domestic market and one-third export market. Unofficial employment estimates in computer software and computer service occupations, including employment by

users, ranged anywhere from 7,000 to 20,000 employees for the same period.

Table 4 lists India's top 14 computer software and service firms ranked by annual sales. With the exception of CMC and NITT, which serve principally as captive suppliers for the Indian public sector and have almost no exports, all other major firms are active exporters. Under a policy established in the mid-1980s, Indian software firms have been encouraged to export software by being allowed to import the needed hardware free of tariffs, as long as the hardware is used in some set proportion in the production of exports. In addition, software exporters benefit from much relaxed foreign exchange controls. Indeed, under an ambitious plan to continue boosting exports, the government is expecting to see export sales triple within two years from their 1988-1989 level. The industry's assessment is more guarded, however, pointing to the fact that such a target is unlikely to be met, simply because of a lack of trained personnel.

Table 4 shows that 12 of the 14 firms are Indian. One firm, Tata Unisys Ltd, is a joint venture between one of India's largest industrial conglomerates and United States computer manufacturer UNISYS. The last firm, Citicorp Overseas Software Limited (COSL), is a fully owned subsidiary of United States banking giant Citicorp.

COSL was formed in 1985 under an Indian Government policy that allows foreign firms to establish fully owned computer engineering and software subsidiaries as long as they engage exclusively in export production. Such subsidiaries have been established by a few other foreign firms, mostly in hardware design (Texas Instruments, for example, has a large facility in Bangalore specializing in computer chip design). In software, however, so far only COSL has seized on this opportunity. Note that while at first COSL's assignments included exclusively captive business from Citicorp, today that share of its business has dropped to about 30 per cent of the firm's annual revenue, owing to the firm's success in developing a roster of external clients.

Until recently, the bulk of Indian software exports came principally from body-shopping, with Indian software firms sending large numbers of systems analysts and programmers overseas to work on projects managed by clients. This explains the high number of

expatriates employed by some of the large Indian software exporters such as TCS, Tata Unisys, or Hinditron (column 6 in Table 4). In recent years, however, Indian software exporters have successfully repatriated some of these overseas assignments and have increased the share of contract programming assignments carried out locally on an export platform basis. The build up of a locally-based export production capacity has also been reinforced by the success of Indian firms at increasing their work as prime contractors (mostly in the area of software conversion) and by recent moves in the packaged applications market. For example, TCS has had some success with a few accounting software packages; Tata Unisys with a signature verification software package for the banking industry; and COSL with several banking software products.

TCS estimates that in 1988-1989, approximately 25 to 30 per cent of its export sales came from turnkey projects, 5 per cent from packaged software, and 65 per cent from "consulting" (body-shopping), compared to nearly 95 per cent from consulting in 1978. COSL's estimates for 1988-1989 show that between 50 and 60 per cent of its sales (all exports) came from turnkey projects, between 30 and 40 per cent from packaged software, and the balance - less than 10 per cent - from consulting services. At Tata Unisys, the estimated percentage breakdown of export sales for 1988-1989 was roughly similar to that of TCS.

As noted earlier, the shift to turnkey work and packaged applications has allowed firms to repatriate part of the employment creation effect resulting from exports, mostly to export zones specially created by the Indian Government in the mid-1980s, as part of a package of incentives introduced to encourage Indian high-tech industries to export (see column 7 in Table 4).

Up to now, exports of Indian software firms have been directed mostly at the United States market, to a lesser extent at the Western European market, and very minimally at the Japanese market. *Computers and Communications,* one of India's leading industry publications, has suggested that Indian exporters would be well served by turning their attention to the Japanese market where labour shortages are even greater than in the United States and where a much tighter immigration policy would likely considerably reduce the sizeable

personnel leakage currently experienced with the United States because of Indian software professionals often remaining in the United States.[8]

Indeed, another way in which India exports its software expertise, but one for which there are no data, is through remittances from software professionals who have migrated abroad, mostly to the United States and the United Kingdom.

Aside from the export market, which has received special attention from the Indian Government, the development of the Indian domestic market remains hindered by the relatively small base of installed computers, especially mini and mainframe computers on which most major applications continue to be developed. As of late 1988, there were at most 70,000 computers throughout the country, most of which were IBM-AT compatibles or lower range PC clones - hardly the kind of equipment needed to develop large-scale applications. India was hurt both by the departure of IBM in the late 1970s and by restrictions imposed by Western governments on the import of computer equipment due to India's long-term relationship to the Eastern block. In addition, India probably has hurt itself with a policy of high tariffs on imported hardware as well as a policy of domestic production of PC-clones that has worked against the build-up of sizeable economies of scale, in a business which is fundamentally a commodity business and for which achieving large economies of scale is the quintessential requirement to lowering prices. More than one observer of the local industry interviewed for this study agreed that it will take some effort to eliminate a number of these bottlenecks before the Indian domestic market can truly take off. One big hope, however, is that DEC's recently opened facility in Goa, where VAX machines are being assembled, will help alleviate some of the bottlenecks in the minicomputer area.

B. Singapore

In the six years between 1982 and 1988, annual computer software and service revenue (external domestic market plus exports) in Singapore more than quadrupled from Sing.$72 million to Sing.$314

8 *Op. cit.*, July 1989. Estimates of current shortages in information technology professionals in Japan run as high as one million (and two million by year 2000).

million. Underlying this large increase were remarkable 25 per cent or more annual rates of growth in the industry during most of the 1980s. Not surprisingly then, by the end of the 1980s the City-State was possibly one of the most computerized nations in the world.[9]

Behind this development lies a highly focused policy by Singapore's government, going back to the early 1980s, to transform the country into a computer-intensive economy. Established in 1981, the National Computer Board (NCB), a public sector agency under the Ministry of Finance, spearheaded the effort during the 1980s by promoting the use of computer technology by all sectors of the economy, the development of a strong local hardware and software industry, the development of a strong computer professional labour force, computer literacy across the entire labour force, and the diffusion of computer applications within Singapore's public sector itself.[10] Indeed, with nearly 700 computer staff, the NCB is itself the largest software enterprise in Singapore.

While no exact figure on the number of software firms in Singapore is available, perhaps as many as 200 firms developed computer software, offered computer services, or at least distributed software packages in 1988, based on reasonable estimates derived from the NCB's latest survey of Singapore's information technology industry.[11]

In 1988, Singapore exported Sing.$56 million worth of computer software and computer services (Table 5). It must be noted that, in addition to direct exports, this figure includes overseas sales by foreign affiliates of Singaporean software firms. Nevertheless, the figure is indicative of the significant presence of Singapore's firms in foreign markets, especially when compared to the industry's total annual revenue of Sing.$313 million for the same year (external domestic expenditures plus exports, see Table 6). Malaysia, the People's Republic of China, ASEAN countries, as well as Western Europe and the United States account for the bulk of Singapore's foreign sales. Domestically, private

9 National Computer Board, *Singapore IT Survey 1989* (Singapore, NCB, 1989).

10 National Computer Board, *NCB Year Book, Fiscal Year 1988/89*, (Singapore, NCB, 1989).

11 National Computer Board, *Singapore IT Survey 1989: "Industry" Report* (Singapore, NCB, 1989).

sector service firms such as banks, brokerage houses, trading firms, and construction-engineering companies, as well as public sector agencies are among the most avid users of computer software and computer services.

Table 7 lists the 26 largest computer software and service firms in Singapore in 1989. The table, when compared to Table 4 containing data for India or similar tables shown later for the other three countries, is highly suggestive of Singapore's remarkable success in developing a sizeable software industry in just a few years, despite its limited human resources due to its small size (approximately 2.5 million inhabitants).

The table also suggests the importance of foreign firms in the local market, with seven of the top 26 firms affiliated with a foreign firm. Of course, this does not reflect the full extent of the presence of foreign firms in the Singaporean domestic market. Foreign firms also sell through direct imports. Unfortunately, the NCB does not produce detailed estimates of software imports into Singapore's market.[12] Singapore does not restrict imports however, and there is ample casual evidence that almost every major mainframe and minicomputer applications package can be purchased from a vendor in Singapore.

Finally, Table 7 also illustrates the extent of the internationalization of some of the local firms themselves. Many of the top firms have sales or production offices overseas (only those for which I collected detailed data are annotated in Table 5). In general, because of Singapore's shortage of computer personnel, when moving overseas, Singaporean firms have tended to focus on activities that either utilize local labour or necessitate very little expatriate Singaporean labour. Firms such as Singapore Computer Software or Information Engineering Software, which specialize in turnkey projects, have developed networks of overseas offices, mostly throughout the Asia-Pacific region, from which they serve local accounts. These offices are primarily staffed with local labour. Other firms, such as CSA Research and ATS Computer Center Pte Ltd. have focused on selling packaged software either through local and overseas dealers and distributors or, if needed,

12 The estimates of Singapore software imports shown in table 3 are mine, and are based on the assumption of an import ratio in Singapore similar to that for the Republic of Korea.

through their own sales offices, but in both cases necessitating little expatriate labour. It should be noted here that the kind of packaged software being developed by some of the Singaporean firms is fairly complex software. CSA Research, for example, offers CASE tool software and ATS Computer Center Pte Ltd. offers CAD and CAE software that run on personal computers work stations. Additionally, a few Singaporean software firms are developing artificial intelligence applications packages.

A final indication of the degree of development of Singapore's software industry can be found in some of its relationships with a few foreign markets. Similar to the software industry in several advanced economies, Singapore is already at a stage where it seeks to attract foreign computer professionals (mostly from Malaysia but also from China and India), and where a number of its firms use overseas subcontractors (from Malaysia, China, and the Philippines) to compensate for local shortages. The latter, as discussed later in this paper, assumes a level of technological sophistication in the area of project development management that is still rarely found among firms from developing countries.

C. The Philippines

Like India, the Philippines is a country rich in human resources and is trying to use its large pool of educated labour as a foundation on which to build a sizeable computer software and service export business. Also like India, the Philippines is finding that it takes time, agility, and resources to transform the country's software industry into a major world player. This being said, the country's accomplishments up to now are not to be underestimated.

Data on the size of the Filipino software industry are extremely limited. The estimates presented in Table 8 are my own and are based on a few available output measures, some employment estimates, as well as some measures of installed computer capacity.

In 1988, the external market for computer software (domestic market and exports) was estimated at about $10 million. Following a downturn in the second half of 1989 in not only the Filipino software industry but also in the national economy, the estimate is that the in-

dustry output will grow to be anywhere between $10 and $20 million in 1990 but may not grow much beyond where it was nearly two years ago.

The conventional wisdom is that external demand for software is split roughly evenly between domestic demand and exports, and that between 50 and 60 per cent of domestic demand is filled by imports of operating and applications software, overwhelmingly from the United States.[13] The external market for computer software is complemented by internal software production by users, perhaps twice as large as the external market in both employment and value, owing to the fact that software development in the Philippines is an activity that remains highly internalized by users.

The bulk of Filipino software exports involves contract programming services. While a share of the export revenue is generated by sending Filipino software professionals overseas, perhaps to a greater extent than in the case of India the industry tries to export principally by producing software locally on an export-platform basis. This is done both by Filipino firms and by foreign firms established locally, working on overseas jobs as subcontractors. As indicated in Table 9, five of the top 20 firms are foreign-linked: two with European companies, two with Japanese companies, and one with a United States firm - namely SGV-Arthur Andersen. As it turns out, the latter also happens to be the largest software firm in the Philippines, employing nearly 500 people, including about 350 working on domestic assignments and 150 on overseas assignments.[14]

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13 "The Philippine Computer Industry", in *Philippine Computer Society Yearbook 1989* (Manila, The Philippine Computer Society, 1989), pp. 26-31.

14 SGV & Co - SyCip, Gorres, Velayo & Co. - is a long and well established accounting service firm based in Manila. The firm remained independent until the mid-1980s, keeping simply a correspondent relationship with Arthur Andersen. By the early 1980s, SGV had grown to become the largest professional service firm in the ASEAN region, employing several thousand professionals. By the mid-1980s, however, the firm's partners assessed that the firm would need a bigger world-wide presence if it were to continue growing and arranged a merger with Arthur Andersen & Co. Since then, Arthur Andersen has helped SGV build sizeable resources in computer services, a business in which Arthur Andersen has built a formidable presence. In addition to working on local assignments, SGV Manila has become one centre in a network of software production facilities, that also includes centres in Paris and in several cities in the United States, from which Arthur Andersen Consulting - the systems-integration arm of Arthur Andersen & Co. - sources software jobs needed for some of its systems- integration assignments.

The Philippines export software to clients in many countries around the world including other ASEAN countries and Australia, but the main receiving countries are clearly Japan and the United States.Filipino firms are also doing a growing volume of business with European clients. As regards Japan, it must be noted that in addition to the two Japanese companies with a local presence, several Japanese software and hardware producers have subcontracting relationships with local Filipino firms, principally to develop software for the non-Japanese market. One Japanese hardware manufacturer even subcontracts software work to one of the non-Japanese foreign-linked firms established in Manila. Of all the countries visited for this study, the Philippines seems to be the place where Japanese software firms have so far established their strongest overseas presence, principally for the purpose of meeting domestic needs. To stay with this point, it must also be noted that the Japanese presence in the region is clearly quite different from the United States presence. While a number of United States firms have been driven to establish a presence in the region by domestic labour shortages and operate there for the purpose of sourcing United States jobs, the United States presence in the region is aimed principally at serving local clients. From the viewpoint of setting national policy, this point may be important to keep in mind when trying to assess varying degrees of commitment by different players to the development of local resources.

In addition to its software industry, the Philippines has a dynamic data-entry/data processing industry that serves both the domestic and export market. As in the case of the software industry, available measures of the industry are quite limited and the estimates presented in Table 8 should be regarded with great caution.

As in the case of the software industry, the build-up of data-entry/data processing exports seems to have taken shape mostly during the 1980s. An accepted wisdom is that the Philippines has actually taken away some of the Republic of Korea's earlier data-entry/processing export business, partly because Korea has gradually priced itself out of the market and partly because of a rapid build-up of resources in the Philippines, complemented by a generous programme of tax incentives. A reasonable estimate is that approximately 5,000 Filipinos work on data-entry/data processing export busi-

ness, generating anywhere between \$12.5 and \$25 million in export revenue. Almost all data-entry/processing firms are Filipino firms, including many that are subsidiaries of Filipino software firms (see Table 10). A large share of the work carried out by the largest firms is for export.

The Philippines export yet a third kind of computer software and computer services, namely the services of computer professionals who move abroad to take up assignments for overseas firms. Typically, these individuals generate remittances for relatives back home - another form of exports for the country. In 1987, slightly over 380,000 Filipinos were deployed overseas to work under short-term employment contracts of all kinds, more than twice the number of those who did so in the early 1980s (this number excludes Filipinos who have taken up long-term residency in other countries but who might also generate remittances for relatives back home). While until the mid-1980s the great majority of those going to work overseas were production or service workers, beginning around that time there was a surge in the number of professionals working overseas under contracts. According to unpublished statistics released by the Philippine Overseas Employment Administration for this study, the number of contract computer professionals deployed overseas could be estimated at approximately 300 in 1986, 600 in 1987, and 800 in 1988.

The Government of the Philippines has ambitious plans to expand rapidly the country's export business in computer software and computer services. Targets of well over \$100 million worth of exports have been mentioned for 1992. The industry association is much more cautious in its assessment however, and suggests that it will take longer to reach that target, rightly pointing to some of the current limitations.

For example, there may be up to 20,000 computer professionals currently employed in the industry (see Table 8). However, meeting the government target might easily demand that this number triple. But while there are many schools and training institutions that offer courses in basic programming or computer language uses, the country still falls short in full-fledged university-level programmes in computer sciences that are needed to form high-level staff.

In addition, the domestic software market remains vastly underdeveloped, partly because of a relatively small installed computer capacity. By early 1990, there were at most 1,000 mainframe and minicomputers installed throughout the country, complemented by perhaps up to 25,000 microcomputers.

One criticism is that the public sector has yet to take a strong lead in the drive toward computerization in the Philippines. While the Government has released a National Information Technology Plan, one assessment is that a strong commitment to the computerization of the public sector itself might do much to build domestic software capacity. The hope is that such commitment will come sooner rather than later.

D. Hong Kong

Together with Singapore and Japan, Hong Kong is one of the most mature markets for computer software and computer services in the Asia-Pacific region, owing to the sophistication of its local customers. Unlike Singapore or Japan, however, Hong Kong has no policy - explicit or implicit - aimed at fostering the growth of a local software capacity. The local government sector has been computerizing its operations for quite some time now, but no particular attempt is being made to incorporate these efforts into a larger-scale plan to promote the development of computerization in the Territory. As a result, Hong Kong's public sector is probably not quite as computerized as is Singapore's.

The only explicit public policy for software services is an annual operating subsidy by the Hong Kong Government to the Hong Kong Productivity Council whose mission is to promote business development in the Territory. The Council employs approximately 60 computer professionals who assist medium- and small-sized firms in the introduction of computerized technologies (for instance, the introduction of computerized garment design in the apparel industry).

Although some of the local firms do export and/or have build an international presence, there is no strong drive by Hong Kong software firms to build a sizeable export capacity. This is because in an industry in which labour shortages are rampant almost everywhere, the situation is even worse in Hong Kong.

Research Asia Ltd. estimates that the market for computer software and computer services in Hong Kong (external domestic expenditures plus exports) was worth approximately $185 million in 1989, up from $150 million in 1988. About two-thirds of the market was served by independent software houses and one-third by hardware vendors (Table 11).

Using output data developed by Research Asia, employment data from the 1987 Manpower Survey Report on the Electronic Data Processing Industry,[15] and limited wage data obtained through interviews, I estimate that total domestic expenditures (internal and external) plus exports of computer software and computer services in Hong Kong was about $700 million in 1989, with over 15,000 workers employed in computer occupations. If my estimate is correct, it would suggest a degree of externalization of user demand for software much lower in Hong Kong than in the other countries (about one fourth of the expenditure, rather than one half). This would seem consistent with the notion that Hong Kong's biggest users of large computer systems are mostly the banks, along with the local utilities, the telephone company, and a few large trading and transportation companies. As the work by Research Asia Ltd. suggests, banks in Hong Kong, perhaps more than elsewhere, have tended to develop their systems mostly in-house. Assistance from independent software houses, when sought, has been mostly on a subcontracting basis.[16] This may also explain why, when compared to Singapore, the population of Hong Kong-based independent software houses is not much bigger, even though total software expenditures may be twice as large in the Territory than it is in the City-State (see Table 12).

Of course, this takes nothing away from the technical competence of computer personnel employed by both independent houses and computer users in Hong Kong, obviously quite high. Citicorp, for example, uses Hong Kong as the primary centre for new systems development for the Asia-Pacific region. Likewise, large multinational

15 *1987 Manpower Survey Report on the Electronic Data Processing Industry* (Hong Kong, The Committee on Electronic Data Processing of the Vocational Training Council, 1988).

16 Research Asia Ltd., *Hong Kong Computer Software Industry Sector Analysis* (Hong Kong, Research Asia, November 1989).

software firms such as Computer Power (Australia) and Logica Technology Services (United Kingdom) use Hong Kong partly as a regional base (see Table 12).

E. Republic of Korea

Like Hong Kong, but for somewhat different reasons, the Korean software industry is overwhelmingly preoccupied with serving the needs of domestic customers, and is little concerned with serving export markets. This does not mean that there is no interest in Korea in exporting software, but simply that the domestic labour shortages of computer professionals are so great in the face of rapidly surging demand for computer software and computer services that the industry cannot even keep up with local customers. Still some firms are developing software packages that could be exported, particularly in the area of utilities software that could be sold in conjunction with hardware produced in Korea (printers, PC-compatibles, etc.).

Demand for computer software and computer services remained quite small in Korea until the mid-1980s, at which point demand exploded. Between 1987 and 1990, external expenditures for software is expected to nearly triple from $300 to about $800 million (Table 13). Together with users, independent software houses and hardware manufacturers are estimated to be employing already over 30,000 software professionals, with an appetite for more. The main actors behind the explosion of software in Korea are two: the public sector and private industry (manufacturing).

With the rapid rise of Korean wages in the second half of the 1980s, Korea suddenly found itself confronted with the erosion of one of its earlier key competitive advantages, namely cheap labour. It did not take long for Korean entrepreneurs to realize that maintaining their competitiveness in world markets would necessitate, at a minimum, boosting productivity on the factory floor. This became the foundation for a drive toward factory automation which has generated a great deal of demand for both hardware and software in Korea.

Paralleling this development, the public sector has become increasingly aware of the need to foster computerization throughout the Korean economy, in part by using public sector agencies as an arena for

the development of large-scale software projects. The Government helped initiate the development of the "Olympics Support" system for the 1986 Asian games, followed by the development of an enhanced version for the 1988 Olympic games. More recently, the Korean Government has launched the National Administration Information System project which will lead to the development of five large-scale computerized on-line data base systems for public sector agencies. The Korean government is also funding R & D efforts, in particular at the university level through KIST - Korea's Institute of Science and Technology.

Perhaps one of the most interesting features of Korea's efforts in the development of its software capacity is its use of relationships that enhance local software capabilities. For example, the Korean Government is heavily promoting the use of joint ventures and other linkages between global software firms and local companies. Thus, EDS has a joint venture with Lucky Goldstar, Samsung with IBM, Hyosung Industries with Hitachi. The large accounting firms also have local linkages: Arthur Young, Coopers & Lybrand, and Arthur Andersen to name a few (see Table 14). Korea is also using the Theater Automated Command and Control Information Management System (TACCIMS), a joint project to improve interoperability between the armies of the United States and the Republic of Korea in order to transfer software know-how. TRW, a leading United States system integrator, is prime contractor on the project, but there are extensive subcontracting relationships with local software houses. Clearly, Korea's software industry has already made use of these transfers of know-how to move up the software field. In addition to work on utilities software mentioned earlier, several firms are working on artificial intelligence software.

There is every indication that Korea's software industry will continue to grow very fast both in size and in sophistication in the years ahead. Not unlikely it will soon become the largest national market in the region outside Japan. The only limitations on the development of the Korean market, it would seem, may have to do both with the rapidity with which the Korean educational system can prepare new computer professionals and perhaps, also, with the extent to which the Chebol structure of the Korean economy may hinder the development of a truly efficient software industry in the future. Under the current

Korean system, where many of the software houses are linked to a particular industrial conglomerate, it often appears to the outside observer that the Korean software industry works more like a set of mini-software industries walled off from each other, with each Chebol channelling business principally to its own software houses, rather than as an integrated software industry. If the experience of the software industry in other countries is an indication of the importance of subcontracting relationships among software firms themselves as key regulatory mechanisms of demand and supply for both labour and expertise, the system that currently exist in Korea, which limits subcontracting relationships among software firms, may, at some point, become somewhat dysfunctional.

IV. BARRIERS TO TRADE

This and the following sections of this report focus on impediments to trade, competitive weaknesses, and competitive advantages as they apply to computer software and computer service firms from the five countries examined in this study. Impediments or barriers to trade refer to restrictions placed by national governments on international transactions; competitive advantages and competitive weaknesses apply to the structural advantages or disadvantages of firms that are rooted in their market of origin, in their business practice, or in the business practices of other firms.

There is no evidence that the barriers to trade confronted by the computer software and service firms from the five countries are any different from those confronted by similar firms from other countries, except perhaps in emphasis. In an earlier paper, I reviewed many of the barriers confronted by a broad range of business services, including computer software and computer services.[17] In this report I restrict myself to a presentation of a short list of key barriers to trade confronted by firms from the five countries, with an emphasis on the form they take within the region, in Western Europe, and in the United

17 Thierry Noyelle, "Business Services and the Uruguay Round Negotiations on Trade in Services", in *Trade in Services: Sectoral Issues* (United Nations Publication, UNCTAD/ITP/26), pp. 309-63.

States, where most of the software exports from the five countries are flowing to.

A. Equity ownership

Many countries in the region restrict local presence of foreign software firms to minority ownership. This is true in Malaysia - where the policy is designed to encourage the increasing participation of bumiputras (indigenous ethnic population) in the economic life of the country - and also in Indonesia, Thailand, Brunei, Burma, Taiwan, Korea, and India. Of course, equity restrictions do vary from country to country. In Thailand, for example, computer software and service firms are classified under Annex C of the Announcement of the National Executive Council No. 281, regulating foreign direct investment.[18] Foreign investors may be empowered by the Director General of the Department of Trade Regulation to engage in business classified in Annex C, but typically the Director General will require Thai equity participation and place restrictions on the number of expatriate managers. Likewise, as noted earlier, India restricts foreign ownership of software firms except in the case of firms established to produce exclusively for the export market.

The exceptions to the regional trend toward restricting equity ownership are Singapore, Hong Kong, and the Philippines. While the Philippines restricts foreign ownership in some sectors of its economy, and in some cases altogether forbids it (for example, in retailing), those restrictions do not apply to the software sector.[19]

Most key countries in Western Europe and the United States do not restrict foreign ownership in the software industry.

B. Content requirements

Almost every country in the region uses and develops principally English software, complemented by some use of software in the ap-

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18 *Announcement at the National Executive Council, No. 281*, originally published in *Government Gazette*, Volume 89, Part 180, 25 November 1972, Thailand.

19 Philippine Board of Investments, *Primer on Foreign Investment Policies in the Philippines* (Manila, Philippines Board of Investments, 1988).

propriate local language (especially for word processing and office automation applications). As far as I was able to determine, only Thailand imposes a requirement that all software developed locally offer Thai screens (i.e. that the computer screens available to the user of the software be written in Thai language).

C. Public sector procurement

Most countries, *de facto* or *de jure,* favour locally owned firms over foreign suppliers (importers or local affiliates of foreign firms) in their procurement of public sector contracts. This is true not only of most countries throughout the region - with the exception of Singapore and Hong Kong which seem far more open than most - but also of most Western European nations, the United States, and Japan.

In practice, however, the policy must often be matched with the reality of meeting needs. As a result, countries such as the Philippines and Korea display a great deal of pragmatism and do not hesitate to turn to foreign suppliers in order to procure contracts whenever need cannot be met adequately by local firms. India is far more restrictive, in this respect, however.

D. Income repatriation and foreign exchange controls

Most countries in the region liberalized their financial markets during the 1980s. This has made it easier for foreign firms to repatriate profits from their overseas operations and for computer professionals to move about the region and develop business with sufficient foreign exchange to cover development costs, costs of travel, and other charges.

On the issue of foreign exchange and income repatriation, India remains the most restrictive of the five countries (Singapore and Hong Kong are the most liberal) although in the case of foreign firms establishing export-only software operations, there are virtually no restrictions. Also, India has relaxed its foreign exchange regulations in recent years, making it much easier for its own exporters to use foreign exchange and travel overseas to prospect for new business or to carry out assignments.

There are no restrictions on foreign exchange and income repatriation in virtually all Western European countries, and no restrictions in the United States.

E. Visas

Under the current system, that is in the absence of a multilateral trade agreement covering temporary migration, countries are largely free to issue visas and work permits as they please. As a result, restrictions on the issuance of visas and/or work permits to software professionals seeking entry into a country for purpose of conducting business is a problem in many countries. The problem seems to have particularly serious impact on Indian or Filipino firms selling contract programming and body-shopping services to United States clients, the predominant users of such services. The United States has a highly discretionary visa policy owing to its fear that temporary professionals will use their temporary stay to establish permanent residence. Western European countries seem more relaxed about the issue, perhaps because they are less likely to be targets for long-term immigration by professionals from the two countries. As for Japan, while there is evidence of growing demand for body-shopping in Japan, the number of individuals involved remains small. However, Japan is known for watching immigration very carefully.

The problem is not limited to contract programming and body shopping, however. There is extensive evidence that most governments in the region encourage foreign firms specializing in turnkey work and custom software to restrict the number of expatriates they bring in to staff branch operations. For example, the Philippine 1987 Foreign Direct Investment Code has a section to that effect.[20] In Thailand, as noted earlier, this is left to the discretion of the Director General of the Department of Trade Registration for most business.[21]

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20 *Primer on Foreign Investment Policies in the Philippines, op. cit.*

21 *Announcement of the National Executive Council, op. cit.*

F. Government subsidies and incentives

To a varying degree, many countries in the region, including the five countries studied here, subsidize firms either by providing patient capital at rates below market rates, by providing tax incentives, by financing R & D programmes, or even through direct operating subsidies. But this is true also of Western Europe, the United States, and, for that matter, Japan, all of whom also subsidize software R & D heavily (in the EC, through programmes such as Esprit; in the United States, principally through military procurement of software; in Japan, through the Fifth Generation Language and SIGMA projects).

Casual observation would tend to suggest that tax incentives usually are accorded relatively evenly between locally owned and foreign-owned firms. Singapore, the Philippines, and India, for example, offer various kinds of tax incentives or tax-holiday schemes to both locally owned and foreign-owned firms. Typically, tax incentives are used either to attract foreign investors or to boost exports. By comparison, R & D subsidies, capital subsidies, and other subsidies are often targeted to domestic firms (Singapore and Korea being the most interventionist of the group in this respect).

The extent to which a country's subsidies are fair or unfair is an issue which is likely to be taken up as part of the negotiation on liberalizing trade in services. As of this writing, the indication is that a specific agreement on subsidies is unlikely to be included in the umbrella agreement on services to be prepared by the end of 1990, but rather that it will be negotiated after 1990. Independent of this issue of timing, it is clear that subsidies in software will become a negotiating issue. If anything, the following example is an indication of this. In early 1990, one United States software company petitioned the United States Department of Commerce to apply countervailing duties to software sold in the United States by a Singaporean company on the grounds that research and development of that product had been subsidized by the Singaporean Government. (In part, the case was being made that since software is transported on a disk it can be taxed as a good.) While the United States Department of Commerce ultimately ruled that countervailing duties were not warranted in this particular case, such

determination by the Department of Commerce would have resulted in imposing a 15.25 per cent duty on the Singaporean software.[22]

V. COMPETITIVE WEAKNESSES AND COMPETITIVE ADVANTAGES

Unlike trade barriers that tend to apply evenly to all foreign firms, regardless of their country of origin, software firms from the five countries, when operating overseas or even within their domestic market, must cope with certain competitive weaknesses that are inherent in the very market from which they originate or in the business practices of firms from other countries. At the same time, they may also benefit from certain competitive advantages linked to their origins. This section reviews both competitive weaknesses and competitive advantages from the vantage point of the firms from the five countries studied here.

A. Small domestic market

In all cases, the small size of the five domestic markets is in itself a competitive disadvantage. Firms originating from these countries do not benefit from the scale economies that are available to firms from larger markets. Scale economies are important in shouldering, for example, the development costs of a software package, staff development costs, the purchase of equipment, and so forth.

B. Cost of foreign presence

The cost of establishing a foreign presence by, say, a Filipino firm in the United States is infinitely higher for that firm than for a United States firm wanting to establish a presence in the Philippines. While barriers to entry (in the economic sense of the term) are very low in the software industry, the cost of sustaining a presence in a major developed country is likely to be very high for a firm from a developing nation, unless the foreign office can become revenue producing almost instantly. That, of course, is very unlikely, especially if the mission of the

22 *Federal Register*, Vol. 55 (17 January 1990), p. 1596, and Vol. 55 (2 April 1990), p. 12248.

commercial presence is to sell packaged software, which typically needs some lead time before generating sales. This may be less of a problem in the case of custom-built software and systems integration work where the firm may wait until it has developed assignments before opening a local office.

C. Discrimination by large software distributors

For a firm from a developing country, problems associated with the high cost of maintaining a foreign presence are compounded by limitations placed on its access to existing channels of distribution. As mentioned earlier, the current software distribution system is dominated by the big hardware manufacturers and a few very large independent software houses (Computer Associates and Cullinet, which have now merged, McCormack and Dodge, a subsidiary of Dun & Bradstreet Business Information Services Division, MSA International, and a few others), most of which are United States or Western European firms. In addition to distributing products from third-party vendors, most of these firms also sell their own applications and will not hesitate to discriminate in favour of their own products. Whenever a small, independent software house succeeds in establishing a successful product, the big distributors will not hesitate to buy it outright, rather than compete with it. This is how Computer Associates has built itself into a giant and how other large distributors (e.g. Dun & Bradstreet) gained market shares during the 1980s. As the demand for computers and therefore the demand for software slows down in the early 1990s in both the United States and Western Europe, competition in the software industry is likely to intensify and the largest players will hold a major advantage by virtue of their size.

D. Cultural stereotypes and lack of business clout

In selling in developed markets, firms from developing countries must often work hard to break through cultural stereotypes and establish their business credibility in areas of quality, continuity, and customer service.

In this respect, a special problem mentioned by firms in several countries is that of the "chauvinism of United States users". The com-

plaint is that United States computer users (by far the largest market) tend to be very parochial in their buying habits, typically favouring "made in America" software over imports.

E. Discrimination by equipment vendors

Discrimination by equipment vendors is another area which affects the competitive position of software firms from developing countries, especially firms specializing in systems integration and turnkey systems.

As explained earlier, a systems-integrator firm typically purchases equipment from a vendor, which it incorporates with software and then resells to its client as a complete system. In order to bid on projects, small systems integrators must establish relationships with local vendors of equipment. Large systems integrators (such as Arthur Andersen, EDS, and others), on the other hand, have established relationships with major vendors throughout the world. In establishing their relationship with new vendors or local distributors, large integrators bring with them considerable clout, and vendors may be willing to sell equipment on terms more favourable than they would give smaller integrators, if only for the purpose of developing a longer-term business relationship with these large integrators. In addition, large manufacturers (e.g. IBM) may give incentives to local dealers to sell equipment to large integrators (e.g. Arthur Andersen, EDS) on favourable terms, if only because these integrators generate a large volume of business. If this is not sufficient, large systems integrators from developed countries have yet another tool at their disposal to purchase equipment on favourable terms. It is called the "list price" effect.

Typically, major hardware manufacturers sell equipment at prices 20 per cent higher outside than within the United States. Large United States systems integrators have extensive relationships with both manufacturers and dealers within the United States. When bidding on a project outside the United States, if local prices are too high, these integrators may use the price differential to demand lower prices from a local vendor, or threaten to purchase the hardware in the United States and import it themselves.

The gist of it all is that when bidding on projects, including outside their home countries, large systems integrators are likely to have a cost advantage on purchased hardware over domestic system integrators. On the other hand, the labour costs of large firms may be higher than those of smaller firms due to higher overhead, higher payscale, or other factors. Thus, in projects that have a high software development component, part of the cost advantage of large firms on the hardware side may be undone by a cost disadvantage on the labour side.

F. Technical Capacity

Competitiveness in the computer software and service industry is both about technical capacity and about labour. By technical capacity, I mean the quality of the firm's labour force, its level of skill formation, and also the firm's expertise and know-how. By labour, I mean both the availability of labour and the cost of labour. To be sure, the smaller the labour cost differential and the tighter the availability of labour, the more important the role of the other factors is likely to be. Still, technical capacity is important even for firms in India or the Philippines, where the advantage derived from the labour cost differential and the availability of labour is greater than in the other countries.

Building technical capacity has two requirements at a minimum: getting access to complex assignments and getting access to advanced technology - both hardware technology and software development technology. Participating in the international market, especially working in the United States or Western European market, is definitely a major way in which firms from developing countries can try to enhance their know-how and expertise through access to complex assignments; it may also be a major way for them to access advanced hardware technology not available domestically. I found ample casual evidence of the latter in the case of both Indian and Filipino firms which, because of limitations in the locally installed computer base, use foreign contracts as a way to access hardware technology. Fostering firm-to-firm technology transfer is another important way in which firms from developing countries may try to boost their level of technical capacity, and, hence their competitiveness. I return to this critical issue in the next section.

G. Labour advantage

This being said, as the experience of the Indian and Filipino industry indicates, firms from developing countries can build a sizeable software export business based in part on the availability and cost advantages of their labour pools. This does not have to be the only basis on which a competitive advantage is built, however, as demonstrated by the experience of Singapore, which has little labour cost or labour availability advantage but instead is building its competitiveness primarily on a high level of skill formation among its computer professionals.

H. Language and proximity to regional markets

Language and proximity to regional markets - both cultural and geographical proximity - is another area that firms can use to build competitive advantages. With the exception of Korea, all of the countries studied here benefit from the widespread use of English which is the dominant language used in software development. All obviously profit enormously from this linguistic advantage, particularly in their dealings with the big European and American markets. They also individually benefit from intraregional linguistic commonalities. Singapore's other major languages are Mandarin and Malay which firms from that country have used to develop business relationships with China and Malaysia. A number of Hong Kong software firms have used their knowledge of Cantonese to develop business in Southern China. Likewise, Korean software firms are building on their linguistic and cultural linkages with Japan to develop relationships with firms from that country.

Local firms also have an advantage over firms from other parts of the world in better understanding regional cultures. As indicated earlier, several Singaporean software firms have established a sizeable office presence throughout the region. There is similar evidence that Indian software firms have used the Indian connection throughout the region, in parts of Africa and even elsewhere, to open up business export opportunities.

VI. PROMOTING DOMESTIC AND EXPORT CAPACITY

There are different ways in which a country can boost its domestic and export software capacity. Measures include software protection, financial incentives, export promotion, and last but not least, the promotion of technology transfer. In this section, I will turn my attention to each of these points, beginning with the last one first.

A. Promoting technology transfer

Aside from the issue of access to hardware, technology development in the software industry works at two levels: skill formation of personnel and development of firm-based know-how.

Skill development of computer software personnel typically occurs in several institutional settings: in colleges and universities, in specialized vocational trade schools, and in firms (software houses, systems divisions of users, and hardware manufacturers). Preparation of lower level computer personnel (data-entry personnel, programmers, and computer operators) is less exacting than that of higher level personnel (systems engineers, systems analysts, and systems designers). Each of the countries included in this study already have extensive networks of specialized vocational trade schools and already offer a number of courses in basic programming at the college level to prepare lower level computer personnel. With the exception of Singapore which has already built (and is expanding) a sizeable roster of specialized computer science programmes at the college and graduate school level, it would be fair to say that the other countries remain resource poor in high-level computer sciences training. This is not to say that they have been complacent about it.

In some countries, such as India and the Philippines, a major problem is the lack of basic computer equipment other than PCs (mini, supermini and mainframe computers) on which to train students in universities. The problem is not as acute in the other three countries. In contrast to the situation in India and the Philippines, Korean universities seem better equipped, and the Korea Institute for Science and

Technology (KIST) even owns a Cray III supercomputer that is available for university-level research and graduate work.

As important as the lack of hardware is the lack of senior industry personnel and senior faculty to teach high-level computer sciences. Part of this deficiency can be and is being made up by sending students overseas to acquire graduate-level university education (mostly to the United States and the United Kingdom). This strategy not only remedies current shortages but also ensures that knowledge transfer takes place in a field that is continuously changing and in which developed countries such as the United States have a lead which they are likely to maintain in the foreseeable future. In the long term, of course, the five countries do need to strengthen their domestic resources in high-level computer science education, partly to satisfy local needs and partly because computer science programmes are one place where advanced R & D work can occur.

Of the five countries visited, Singapore has the most focused higher education system with which to prepare information-technology personnel, partly because it has had the longest commitment to the development of its software sector. The National Computer Board estimates that Singapore's higher education system prepares 600 to 700 new software personnel each year. This includes 350 to 450 graduates from three diploma schools (two-year colleges) and about 250 graduates from one university (three-year and four-year degrees). In addition, approximately 200 Singaporeans graduate from foreign universities. But with a targeted need of 30,000 software professionals by the year 2000, the country needs to produce 2,000 to 2,500 new graduates each year. To that effect, the country is going to increase the output of its existing diploma schools. In addition, it is opening a new university which will be devoted to engineering and physical sciences and which will offer a major programme in computer sciences.

Limits on the availability of senior personnel weigh as heavily on an individual firm's ability to train its own personnel as it does on the ability of universities to prepare a pool of trained labour. Particularly important in this respect is the lack of trained personnel with project management experience. The production of software is a complex process which may involve large teams of people, possibly includ-

ing teams in several locations. The lack of experienced staff can hinder the capacity of a firm to carry out large, complex assignments. As one observer of the Korean scene noted, the local industry is very young, does fairly well in attracting new recruits, but lacks personnel with 10 to 15 years experience. As he put it, "You can't compress 15 years of experience acquired on the job into two or three years".

One way to address this problem is to recognize that patience is warranted and that it will take time for most countries to work their way through this particular bottleneck. In addition, countries also can promote arrangements with foreign firms that encourage bringing in senior project management personnel from overseas. This is one of the objective of Korea's policy of joint ventures between local and foreign software houses. Here it may be important for countries to note that a policy that restricts too tightly the number of foreign expatriates allowed to work in their country may work against the objective of strengthening the domestic capacity of that country in the software and computer service industry.

Countries can also encourage local firms to bring back national expatriates who might have ventured to the United States or Europe a decade or two ago and are now in senior positions in firms in those countries. This is a policy that has been followed by both India and Korea.

Still, technology transfer in the software industry is not only about the preparation of trained personnel; it is also about the transfer of managerial know-how, a form of know-how which goes beyond individual know-how. In the software industry, one such key managerial technology is what is known as "structured methods". Structured methods are procedures to rigorously analyse and design new systems and organize the division of labour between analysts, designers, and programmers, who must write the codes based on the design and documentation developed by others.

Structured methods have been around for many years, but their rigorous utilization, at least by the most advanced firms, has increased sharply in recent years, partly as a means to promote stronger quality control and partly as a means to ensure proper detailed documentation of a programme so that, changes can be introduced more effectively.

As the pressure on user-firms to upgrade software programmes increased during the 1980s, partly because of rapidly changing technology necessitating the migration of old programmes to new operating environments and partly because of market pressures to come up with better software, many users found that less rigorous production of software in the past had made it very difficult to rework some of those programmes.

Structured methods are diffusing also because they are a means to achieve productivity gains in an area in which such gains are hard to come by. This is the case for two reasons. First, there is the emergence of CASE tools, which are the software programmes used to design the software (in large part, they are a means to enforce systematic and consistent documentation of the inner logic of the programme as it is being developed). Second, there are major conceptual changes in the way in which programmes are being designed - in particular the recent shift to object-oriented programming, a software development method that allows for the development of modular programmes in which upgrading can be handled through the addition, replacement, or upgrading of modules without disturbing the integrity of the software, as is the case with more traditional methods of designing software.

This being said, structured methods do vary somewhat based on the type of software under development. In the area of applications software, some firms (e.g. Arthur Andersen) have developed proprietary structured methods; many use structured methods available in the public domain along with commercially available CASE tool packages. Usually firms are not particularly protective about proprietary methods, because the issue is not so much that of having access to specific methods, as it is that of having the managerial rigour to implement them. More importantly, since so much large-scale software development today involves subcontractor relationships, prime contractors will need to ensure that their subcontractors utilize the same structured methods by training them directly. In one very interesting example observed in the Philippines, the Pact Group, an affiliate of a French software firm, was working on a large-scale project to develop a complete freight tracking system for a major European airline. Nearly 20 European software subcontractors were working on the project along with the Manila office. All had been trained by the firm's senior personnel during the first six months of the project in the use of the same

object-oriented structured method - a very large investment on the part of the prime contractor but one that is not unusual in the industry. Senior project managers located in Manila included both local Filipino staff and senior staff brought from France and other European countries.

Another example of method transfer is Arthur Andersen's licensing of its structured method software to the Korean government to be used in the development of applications for the Korean public sector.

What this discussion of the importance of software development skills and know-how suggests is that the development of a domestic software capacity necessitates that countries take a hard look at two issues: first, the positive role that foreign firms either through full-fledged local establishments, through joint ventures, or through other arrangements can play in the transfer of service know-how; and, second, the importance of open labour markets that allow substantial turnover of personnel through the external labour market. Regarding the second point, it is a critical feature of the service sectors of advanced economies that their labour markets are quite open. Such openness allows extensive job-hopping by individuals which serves to transfer skills and know-how from firm to firm through the individuals who change jobs.

This being said, access to hardware is also an important dimension of the transfer of technology in the software industry. The issue has already been mentioned in connection with the lack of hardware at the school and university level. But this is also an issue for firms that may be hindered in their capacity to develop commercial applications because they lack equipment. Still the problem of access to hardware - especially mainframes and minicomputers - is now partly alleviated by the fact that PCs can now be used to emulate larger machines at the software development stage.

B. Financial incentives

Government can promote the development of a local software industry in different ways. With the exception of Hong Kong which tends to have a laissez-faire policy, the other four countries each promote actively the development of their software industry.

Singapore and Korea, and to a lesser extent India and the Philippines, recognize the importance of promoting computerization in the public sector, both as a means to promote the use of computers throughout a large sector of the economy and because public sector computerization projects tend to be large and thus present opportunities for local software firms to learn to develop large-scale projects. As mentioned earlier, Singapore used public-sector computerization as early as 1981 as a flagship for its efforts to computerize the entire economy; through its National Administration Information System (NAIS) project, Korea has five major computerization projects involving key public sector agencies on its drawing board.

In addition, governments can provide financial incentives to local entrepreneurs and foreign firms. Singapore, for example, provides tax abatements to cover training costs, tax incentives for software R & D projects (double deduction), direct R & D subsidies, and attractive office space in its Science and Technology Park.[23] Singapore is using some of these incentives to encourage foreign firms to set up software R & D centres. India has a system of export zones in which firms are freed of most domestic regulations and in which foreign firms are encouraged to start operations. The Philippines has a generous tax-holiday package operated by the Board of Investments, to encourage exports by both domestic and foreign firms.

As was mentioned in the context of the discussion of technology transfer, governments also have an important direct role to play in personnel development by ensuring proper allocation of public resources to computer programming and computer science programmes in schools and universities.

C. Export promotion

In addition to financial incentives, governments can assist in promoting software exports by using different promotional formulas depending on the stage of development of the local industry. In the Philippines, for example, several government agencies, jointly with the

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23 David Sanger, "Singapore's High-Tech Lure", *International Herald Tribune*, 16 May 1990.

Philippines Software Association, organize sales promotion missions to foreign countries for Filipino firms and visits by foreign firms to the Philippines. For instance, in May 1990, the Netherlands Center for the Promotion of Imports from Developing Countries sponsored twelve leading Filipino software firms to participate in the Europe Software'90 exhibition held in Utrecht. This participation had been initiated by the Center for Trade and Expositions (CITEM) of the Department of Trade and Industry of the Philippines. Singapore emphasizes showcasing its products at conventions and exhibitions organized locally but aimed at attracting foreign vendors. Still, one area that could use some creative thinking is in figuring out ways in which developing countries' governments might entice the large distributors of packaged software to distribute the products of their firms.

D. Protecting software

Last, but not least, governments can do much to promote the development of a local software industry by promoting and enforcing copyright protection.[24] It is important, at the outset of any discussion of this highly charged topic, to recognize that developing countries are faced with the challenge of reconciling two conflicting objectives.

Developing a profitable local software industry assumes that proper mechanisms exist to reward the efforts of software developers. If pirates are free to copy and distribute any new software product as soon as it is released, there are simply no economic incentives for software developers to carry on with their work.

While piracy is unmistakably detrimental to the development of the local software industry, it also must be recognized that piracy contributes to the faster diffusion of computer technology throughout society. Large users and software houses throughout the region do acknowledge that PC software piracy - the area where the greatest share of the piracy problem has occurred - helped diffuse the technology much faster than otherwise would have been possible. In turn, rapid

24 For a relatively non-partisan discussion of this complex issue, see United States Congress, Office of Technology Assessment, *Computer Software and Intellectual Property*, Background Paper (Washington, D.C., U.S. Government Printing Office, March 1990).

diffusion of PC technology boosted productivity and created new demand for bigger and more advanced computerized systems, in other words, helped create new demand for software services, as new users discovered the benefits of computer systems.

Part of the conflict between these two views of software protection has to do with the pricing of software, especially PC software. Until recently, the pricing strategy of large software producers outside their home country (mostly the United States) tended to be the same as that of large hardware manufacturers, namely to charge a set percentage above the price charged in the United States market. Needless to say, this made for prices often well out of proportion with the resources of local small business or individual users.

Large software producers have begun to respond to criticism by reassessing their pricing policy. In addition, most countries in the region have either strengthened their copyright laws or strengthened the enforcement of those laws often under pressure not only from United States software producers but also from their own producers.

One solution proposed to put an end to PC software piracy - and one suggested by several executives interviewed in the five countries - would be for developing countries to negotiate "site licensing" agreements with some of the major producers of PC software (e.g. Lotus, Microsoft, Novell) for some of their major products. As universities or companies in developed countries obtain site licenses to use one copy of software simultaneously on more than one computer in return for a flat fee, developing countries might pay a nominal fee to legitimate the dissemination of a particular software throughout their country.

VII. CONCLUSION

Computer software and computer services were among the fastest growing industries worldwide throughout the 1980s. This is likely to remain the case in the decade ahead as more firms in more sectors and more countries computerize in order to improve their productivity and competitiveness.

This study of the development of the computer software and service industry in five Asian developing countries suggests that most software products continue to be produced locally by indigenous software firms or by users themselves. This is the case even in countries such as Hong Kong and Singapore which have placed few restrictions on imports and direct investment by foreign software producers.

While the shift to packaged software and improvement in satellite telecommunications have increased opportunities for "pure" cross-border trade in computer software and computer services, the evidence presented in this report suggests that such imports remain limited when compared to total (external and internal) domestic expenditure. In addition, while a number of multinational software firms are competing directly with indigenous firms in the domestic markets of four of the five countries through local affiliates, such presence is in no way predominant, and there are few reasons to believe that this is about to change. Most software production is a highly labour-intensive process, organized on a short-term, project-oriented basis, with few opportunities for scale economies. These factors make it very unlikely that a few firms can control a large chunk of the industry's labour market anytime in the near future.

Another interesting finding is that opportunities exist for firms from developing nations, based on technical capacity and labour advantages, to export computer software and computer services. While the nature of these exports varies substantially based on the level of development of resources in each country, the record suggests that this is a highly dynamic field and that there are plenty of opportunities for individual countries to upgrade the knowledge intensity of their exports as the industry develops.

Technology transfer is a critical issue in the development of the domestic and export capacity of the computer software and service industry. Technology in the software industry operates at two distinct but equally important levels: manpower preparation and firm know-how. As noted in this report, there are several ways in which technology can be transferred at each of these levels. One point, however, must be noted. In this highly fluid and rapidly changing industry, the evidence suggests that sizeable opportunities exist for transfers of firm know-how in countries that provide access to their domestic market to

a local presence by foreign firms. For this reason, it has been an essential element of the developing countries' position in the Uruguay Rond negotiations that commitments on access to markets may be made conditional upon the acceptance of technology-transfer obligations by foreign suppliers.

Table 1

THE WORLD'S 25 LARGEST SOFTWARE FIRMS, 1989

		Country	Software Revenues (million dollars)
1	IBM	United States	8,424
2	Fujitsu	Japan	1,449
3	Computer Associates	United States	1,290
4	NEC	Japan	1,065
5	UNISYS	United States	875
6	Digital	United States	825
7	Microsoft	United States	821
8	Hitachi	Japan	724
9	Siemens	Fed. Rep. of Germany	638
10	Hewlett Packard	United States	600
11	Nihon UNISYS	United States	587
12	Oracle	United States	554
13	Group Bull	France	517
14	Lotus	United States	516
15	Olivetti	Italy	498
16	Dun & Bradstreet	United States	450
17	Finsiel	Italy	391
18	Sema Group	United Kingdom	379
19	Nixdorf	Fed. Rep. of Germany	372
20	Mentor	United States	334
21	STC	United Kingdom	327
22	CSK	Japan	310
23	Novell	United States	288
24	Sciences Applications	United States	239
25	Apple	United States	163

Source: "Datamation 100", *Datamation*, July 1990.

Table 2

THE WORLD'S 25 LARGEST COMPUTER SERVICE FIRMS, 1989

		Country	Computer Service Revenues ($ million)
1	EDS	United States	2,478
2	ADP	United States	1,690
3	TRW	United States	1,565
4	Computer Service Corp.	United States	1,442
5	Digital	United States	1,387
6	Andersen Consulting	United States	1,226
7	IBM	United States	1,200
8	Cap Gemini/Sogeti	France	1,103
9	NTT	Japan	899
10	UNISYS	United States	825
11	Black & Decker	United States	688
12	American Express	United States	660
13	General Electric	United States	550
14	Martin Marietta	United States	502
15	Ernst & Young	United States	450
16	NCR	United States	425
17	STC	United Kingdom	425
18	Sligos	France	386
19	SD. Scicon	United Kingdom	381
20	British Telecom	United Kingdom	360
21	Boeing	United States	359
22	Kyocera	Japan	359
23	NYNEX	United States	317
24	NEC	Japan	290
25	Finisiel	Italy	271

Source: "Datamation 100", *Datamation*, July 1990

Table 3

COMPUTER SOFTWARE AND SERVICES IN FIVE DEVELOPING ASIAN COUNTRIES, 1989

	Internal and external market		*External market*			
	Users & independent suppliers		*Independent suppliers*	*Exports*	*Imports*	
	Total industry employment	*Total domestic expenditure (external and internal) plus exports million dollars*	*Total domestic external expenditure plus exports million dollars*	*Million dollars*	*Million dollars*	*Employment in foreign-linked firms as percentage of employment in domestic external market* [a]
Philippines (1990 est.) [b]	13,000 - 19,000	60 - 95	35 - 45	17.5 - 35	2.5 - 5 [c]	20.0
Singapore	8,300	340	170	30 [d]	25 - 50 [c]	9.0
Hong Kong	15,300 [e]	700	185	na [f]	25 - 55 [c]	8.5
Korea	30,000	590	288	3 - 7 [g]	40 - 80	15.1
India (1988-89) [b]	7,000 - 20,000	500	300	100 - 90	na [f]	11.0
	73,600 - 92,600	2,200	980	140 - 170	95 - 190 [h]	

Source: Tables 4, 5 - 14.

a Employment in foreign-linked firms (fully-owned foreign affiliates, joint ventures, partnerships) as percentage of employment in external domestic market except for India where ratio of revenues of foreign-linked firms as percentage of external domestic market revenues.
b Includes employment, revenues, and exports of data entry/data processing services.
c Assumes import ratio for Philippines, Singapore, and Hong Kong similar to that for the Republic of Korea.
d Includes sales by foreign affiliates of Singaporian firms.
e 1988 employment estimate. Includes data entry/data processing employment.
f Not available, but small.
g Does not include export of data entry/data processing services.
h Excludes India.

Table 4

LARGEST COMPUTER SOFTWARE AND SERVICES FIRMS IN INDIA, RANKED BY SALES OF COMPUTER SOFTWARE AND SERVICES ONLY, 1988-1989

Rank	Firm	1988-89 Total sales (Rs million)	1988-89 Foreign sales (Rs million)	Total employment	Overseas employment	Export zone employment	Domestic employment	Remarks
1	CMC (Dehli)	900.0	2.0	-	-	-	-	Public sector
2	Tata Consulting Services (Bombay)	450.0	320.0	1,700	500	200	1,000	
3	Tata Unisys Ltd. (Bombay)	290.0	250.0	760	300	400	60	Joint venture with minority interest from UNISYS
4	HCL Ltd. (Bombay)	190.0	-	-	-	-	-	
5	Electronics Corp. of India (Hyderabad)	105.0	-	-	-	-	-	
6	Hinditron (Bombay)	95.0	20.0	220	48	40	132	
7	DCM Data Products (Dehli)	75.0	10.0	-	-	-	-	
8	National Institute of Information Technology (Dehli)	75.0	1.0	-	-	-	-	Public sector
9	Datamatics Consultants (Bombay)	60.0	50.0	-	-	-	-	
10	Citicorp Overseas Software Ltd. (Bombay)	55.0	55.0	200	35	165	0	Fully owned subsidiary of Citicorp
11	Infosys (Bangalore)	32.0	22.0	-	-	-	-	
12	WIPRO (Bangalore)	25.0	2.5	-	-	-	-	
13	OMC Computers Ltd.	20.0	12.0	-	-	-	-	
14	Blue Star Ltd. (Bombay)	12.0	10.0	-	-	-	-	
	Top 14 firms	2,384.0	800 - 900 (estimate)	-	-	-	-	

Source: *C & C Computers and Communications*, Delhi, July 1989; company data.
Note: Computer software and services only. Does not include data entry services.

Table 5

EXPORT MARKET SALES OF COMPUTER SOFTWARE AND SERVICES FROM SINGAPORE, 1988

(Million Singapore dollars)

Mainframe	17
Mini-computer	33
Micro-computer	6
Total	56

Source: National Computer Board, *Singapore IT Survey, 1989*, "Industry".

Table 6

COMPUTER SOFTWARE AND SERVICES (EXTERNAL DOMESTIC CONSUMPTION PLUS EXPORTS) BY MACHINE CONFIGURATION IN SINGAPORE, 1987 AND 1988

	In million Singapore dollars		*Percentage distribution*	
	1987	*1988*	*1987*	*1988*
Mainframe	77	93	31.6	29.7
Mini-computer	133	184	54.5	58.8
Micro-computer	34	36	13.9	11.5
Total	244	313	100.0	100.0

Source: National Computer Board, *Singapore IT Survey*, *"Industry"*.

Table 7

LARGEST SUPPLIERS OF COMPUTER SOFTWARE AND SERVICES IN SINGAPORE AND RANKED BY LOCAL EMPLOYMENT, 1989

Rank	*Firm*	*Total staff*	*Remarks*
1	National Computer Board	700	Public sector agency in charge of developing applications for the public sector.
2	Singapore Computer Systems	500	Overseas (170); sub of Singapore Technologies Industries.
3	CSA/CSA Research	140	CSA Research: United States (20).
4	Information Engineering Services	120	Malaysia (20); China (15); Canada (5); United Kingdom (10); sub of Singapore firm.
5	Asian Computer Services	88	Includes bureau services.
6	Arthur Andersen Consulting	80	Member of Arthur Andersen Worldwide (United States).
7	Electronic Data Systems	77	
8	EDS International (Singapore)	62	Includes facilities management. Fully-owned sub of EDS/General Motors (United States).
9	Coopers & Lybrand Manag. Consult.	60	Member of Coopers & Lybrand International (United States).
10	Far East Computers	59	Subsidiary of Hindustan Ltd. (India).
11	Chartered Electronics Industries	55	
12	ATS Computer Center	51	United Kingdom (8); Philippines (10) and Malaysia (3).
13	Peat Marwick Manag. Consul.	50	Member of KPMG (United States).
14	Computer Processing Services	50	
15	Computer Associates/Cullinet	43	
16	Chungco Technology	37	Fully-owned subsidiary of Computer Associates (United States).
17	Computer Place Services	37	
18	Singapore Engineering Software	36	
19	Primefield	35	
20	BITEC Computer Centre	33	
21	Brushwriter Corp.	33	
22	IPACS	32	
23	Business Decisions Systems	32	
24	Apex Sustems	30	
25	SW International Systems	25	Joint venture ICL (United Kingdom), SW (Australia), local entrepr.
26	Innosys	25	

Source: Singapore Federation of the Computer Industry, *1989/90 Membership Directory; Asian Computer Director, 1990*; Company data.
Note: Includes computer software and services only, unless otherwise indicated. Does not include data-entry firms.

Table 8

COMPUTER SOFTWARE AND DATA PROCESSING SERVICES IN THE PHILIPPINES, 1990 (ESTIMATE)

	External expenditure		*Internal expenditure*
	Exports by independent suppliers	*Independent suppliers*	*Users*
Data processing	$12.5 - 25 million (approx. 5,000 people; 2,500 work stations)	$15 - 25 million (approx. 7,000 people) (mostly users)	
Software and services	$5 - 10 million (approx. 500 to 1,000 people)	$5 - 10 million (approx. 1,000 people)	$20 -25 million (approx. 4,000 to 5,000 people)
Total	$17.5 - 35 million	$40 - 60 million	
	$60 - 95 million employment: 12,000 data entry 7,000 software and services		

Source: Interviews; Philippine Department of Trade and Industry, *Computer Software and Services: Industry Profile*, 1989.

Table 9

LARGEST DATA ENTRY AND ENCODING FIRMS IN THE PHILIPPINES RANKED BY LOCAL EMPLOYMENT, 1989

Rank	*Firm*	*Potential maximum staff*	*Work Stations*	*Remarks*
1	ASEC International Inc.	1,500	420	a
2	Saztec Philippines Inc.	1,000		a
3	Omnidata Computer Corp.	700	350	
4	Equitable Computer Services Inc.	500	250	
5	RP Computer Traders and Services	500	250	
6	Software Ventures International Inc.	500	180	
7	Worldwide Information Service Enter. Inc.	500		a
8	Systems Resources Inc.	330	165	Division of Software Venture Intl., Philippines a
9	ASEC Information Services Inc.	320		a
10	Mega Data Corp./Mega Group of Comp. Co.	250	120	Division of Mega Group of Com. Co., Philippines
11	Unidata Computer Corp.	250	120	Division of Unidata/Uniphil., Philippines a
12	Asian Data Entry Corp. (ADEC)	250		
13	Equidata Philippines Inc.	200	96	a
14	Hexa Corporation	140	69	
15	Sencor	125	52	
16	Chicodata Encoding Corp.	120	60	
17	First International Database Corp.	120	60	a
18	Pacific Data Corporation	120	56	a
19	Share Management Systems Inc.	100	52	
20	System and Data Manager	80		a
21	Data Solutions Inc.	80	52	a
22	Glenpro Database Corp.	60	30	a

Source: Philippines Association of Data Entry Corporations, 1989; Philippines Board of Investment, *Registered Companies*, 1989; *Asian Computer Directory*, 1990; Company data.

Note: Firms are ranked according to potential maximum employment capacity assuming two or two and a half shifts. In 1989, most data entry work by independent suppliers was for the export market. Approximately 4,000 to 5,000 key punchers worked for the export market.

Other large data entry firms include Asian Computer Resources and Services, Chartnet Philippines Inc., Datascope Communications (Phils) Inc., Litigation International Technical Enterprise Inc., Philippines Database and Services, Systems and Encoding Corp., Pasco Certeza Computer Mapping Corp., Systems for Philippines Inc., all BoI-registered. Data for those firms are not available.

a Registered with the Board of Investment (BoI), see text.

Table 10

LARGEST COMPUTER SOFTWARE AND SERVICES SUPPLIERS IN THE PHILIPPINES RANKED BY LOCAL EMPLOYMENT, 1989

Rank	*Firm*	*Total staff*	*Remarks*
1	SGV-Arthur Anderson	480	Member of Arthur Andersen Worldwide (US). [a]
2	Mega Data Corp./Mega Group of Computer	250	Software and bureau services. [a]
3	Systems Resources Inc.	250	Firm has large data entry operation. [a]
4	Software Venture International	200	Firm has large data entry operation. [a]
5	Equitable Computer Services	150	Software and bureau services.
6	Dynasoft	100 [b]	
7	Computer Information Systems Inc.	100 [b]	Subsidiary of Miralco (Philippine electric utility).
8	DBP Data Center Inc.	100 [b]	Subsidiary of Development Bank of Philippines.
9	Ayala Systems Technology Inc. (ASTECH)	100 [b]	Subsidiary of Ayala Group (Philippines). [a]
10	EBG Systems Inc.	84	[a]
11	The Pact Group	70	Subsidiary of SRI (France). [a]
12	Multinational Computer and Communications Assoc.	63	
13	Software Laboratories Inc.	60	
14	Data Systems Services Inc.	53	Subsidiary of First Manila Management Corp. (Philippines). [a]
15	Philippines Business Automation Systems	50	[a]
16	Computer Software Services/ST & A Co.	50	[a]
17	Nixdorf Computer R & D Center	45	Subsidiary of Nixdorf (Germany). [a]
18	Unidata/Uniphil	45	Firm has large data entry operation. [a]
19	Asian Data Entry Corp.	40	Firm has large data entry operation. [a]
20	Programming Impact Philippines	35	[a]
21	TSD Software Inc.	35	Subsidiary of TSD Corp. (Japan). [a]
22	Infoserve	30	
23	Visalayan Electric Co. Inc. EDP	29	Bureau services
24	Online Advanced Systems Corp.	26	Bureau services
25	Decision Systems Corp.	25	
26	Datronics Philippines Inc.	25	Bureau services
27	Republic Business Systems International Inc.	25	

Source: Philippines Software Association, 1989; Philippines Board of Investment, *Registered Companies*, 1990; *Asian Computer Directory, 1990*; Company data

Note: Includes computer software and services only, unless otherwise indicated. Does not include data entry services. Employment in most firms is subject to wide fluctuations as projects end or new ones begin.

a Registered with the Board of Investment.

b Estimate.

Table 11

COMPUTER SOFTWARE AND SERVICES REVENUES (EXTERNAL DOMESTIC EXPENDITURES PLUS EXPORTS) IN HONG KONG, 1988, 1989
(Million dollars)

1989	185
1988	150
Percentage breakdown by type of Producer, 1989	
Software and service houses	68
Hardware vendors	32

Source: Research Asia Ltd., *Hong Kong Computer Software Industry Sector Analysis*, November 1989.

Table 12

LARGEST COMPUTER SOFTWARE AND BUREAU SERVICE SUPPLIERS IN HONG KONG RANKED BY LOCAL EMPLOYMENT, 1989

Rank	*Firm*	*Total staff*	*Overseas offices (employment)/remarks*
1	Computasia	450	Sub. of HK Telecom (Cable & Wireless). Mostly internal use; some external clients.
2	COL Ltd.	220	Includes bureau services and hardware sales. Subsidiary of World Intl. (Hong Kong).
3	T.A. Consultants	150	United States (6); Taiwan (25).
4	Logica Technology Services	75	Includes Malaysia staff. Subsidiary of Logica Plc.(United Kingdom). 3,000 staff world-wide.
5	Wing On Computer Systems	67	Subsidiary of Wing On Group (Hong Kong).
6	Hong Kong Productivity Council	60	Software staff only. Government-owned.
7	MIS Software	50	
8	Armitage Computer Systems	50	
9	CIM Systems	50	
10	Computer Power	50	Subsidiary of Computer Power (Australia). 3;000 staff worldwide.
11	Commercial Software Services	50	Subsidiary of Bangkok Bank (Thailand) and Commercial Bank of Hong Kong (Hong Kong).
12	Australasia Computing Services (HK)	49	Singapore (4).
13	Systems-Pro BCS	47	
14	Arthur Andersen & Co.	43	Member of Arthur Andersen Worldwide (United States).
15	BIS Banking Systems	42	
16	Three Principles Computer Service	40	
17	Sun Computer Systems	40	
18	Onflo Comp Co./Onflo Tech. Service	39	
19	Sanyo Extended Data Systems	35	Subsidiary of Sanyo Securities (Japan).
20	Datacheck	35	
21	Ramus Computer Systems	34	
22	Canton Pacific Systems	30	Subsidiary of Security Pacific Asian Bank (United States).
23	Johnson Computer Consultants	25	
24	Cogitate Computer Soft Sys.	24	
25	Computer Associates/Cullinet	23	Subsidiary of Computer Associates (United States).

Source: *Asian Computer Directory*, 1990. Research Asia Ltd., "Hong Kong Computer Software Industry", November 1989. Company data.
Note: Computer software and services only, unless otherwise indicated. Does not include data entry services.

Table 13

COMPUTER SOFTWARE AND SERVICES REVENUE IN KOREA: INTERNAL AND EXTERNAL DOMESTIC EXPENDITURES PLUS EXPORT SALES, 1987-1989

Korea's software market growth

(Million dollars)

	1987	*1988*	*1989*	*1990* [a]
System software				
OS	13.25	21.86	29.73	45.60
DBMS	12.40	14.46	16.32	20.80
Communications S/W	0.63	1.71	2.45	6.30
Programming language	2.70	4.29	6.54	9.80
Others	0.7	1.30	2.12	5.50
Subtotal	29.68	43.62	57.16	88.0
Application software				
Word processor	1.03	2.09	3.10	4.20
LAN S/W	0.88	1.51	2.75	5.90
CAD/CAM S/W	2.40	3.69	5.89	8.50
MRP	2.49	3.47	4.26	5.60
POS	0.13	0.43	1.23	3.40
AL	-	-	0.7	1.10
Others	4.44	7.77	10.6	15.80
Subtotal	11.37	18.96	28.53	44.50
Computing services				
Computing services (including facility management)	111.25	187.14	201.64	280.00
Self-developed software	151.91	216.47	302.10	366.62
Total	304.21	466.19	589.43	779.12

Source: *Electronics Korea*, March 1990.

a Estimates.

Table 14

LARGEST COMPUTER SOFTWARE AND BUREAU SERVICES IN KOREA RANKED BY LOCAL EMPLOYMENT, 1989

Rank	Firm	Total staff	Sales (thousand dollars)	Remarks (including affiliations)
1	Systems Technology Management Corp.	1,055	63,200	Joint venture 50/50 EDS and Lucky Goldstar. [a]
2	Ssangyong Computer Systems Co.	530	65,000	[a]
3	Samsung Data System Co.	470		Joint venture Samsung (66.6%) and IBM (33.3%) [a].
4	Goldstar Software	400	27,500	[a]
5	POS Data Co.	350	9,550	[a]
6	Korea Information Computing Co.	300	10,450	[a]
7	Korea Information System	298	6,800	[b]
8	Young Hwa Computer Center	298	3,300	Affiliate of Young Hwa/Arthur Young International. [b]
9	Union Systems Inc.	250	17,650	[a]
10	Sammi Computer Service Co.	225	9,700	[a]
11	Mincom Computer Service Co.	210		
12	Hyosung-Hitachi Data Systems	188	10,000	Joint venture of Hyosung Industries/Hitachi. [a]
13	Daewoo Information Systems Co.	147	5,800	
14	Samil Management Consultants Inc.	130	5,400	Affiliate of Samil Accounting/Coopers & Lybrand.
15	International Computer Service Corp.	124	2,500	
16	Yonhi Computer Co.	124	2,200	[b]
17	Jungwoo Electronics & Information Ind.	120	4,850	[a]
18	Taihan Engineering Co.	120	5,300	[c]
19	Byucksan Info. Ind. Co.	116	5,150	[a]
20	New Computer Service Co.	105	10,300	[a]
21	IBM Korea Inc.	100		Estimate for software service personnel only.
22	Korea Techno-Venture Inc.	93	1,650	
23	Kyung Han Systems	86	10,700	[a]
24	Yuyoung Systems Inc.	82	1,450	
25	A-point Data	77	4,450	[a]
26	Systems Korea Co.	75	7,650	[a]
27	Kirin Systems Corp.	74	3,600	[a]
28	Central System R & D	72	3,650	[a]
29	Korea Business Consulting Co.	72	5,600	[a]

Table 14 (Continued)

LARGEST COMPUTER SOFTWARE AND BUREAU SERVICES IN KOREA RANKED BY LOCAL EMPLOYMENT, 1989

Rank	*Firm*	*Total staff*	*Sales (thousand dollars)*	*Remarks (including affiliations)*
30	Korea Computer	67	4,500	1989 software sales only: $ 1.150 million. a
31	Samdo Data Systems	65	1,550	
32	Kyungki System Co.	61	3,350	a
33	Almighty Computer Co.	61	3,650	a
34	Hyundai Engineering Co./Systems Division	na	na	Hyundai Engin. employs 1,500; breakdown, for systems division, not available

Source: Korea Software Industry Association, *1990 Director of Membership*; Company data.
Note: Includes computer software, computer services and bureau services unless otherwise indicated. Does not include data entry services.
a Includes hardware sales.
b Includes data entry operations.
c Includes software sales.

LABOUR MOBILITY, TRADE IN SERVICES AND THE URUGUAY ROUND: THE PERSPECTIVE OF ASEAN COUNTRIES

*Pang Eng Fong and Linda Low**

INTRODUCTION

The liberalization of temporary labour movement is one of many contentious issues that divide developed and developing countries participating in the Group of Negotiations on Services (GNS) in the Uruguay Round of multilateral negotiations. Concerned with the economic and social repercussions of increased international labour flows, developed countries have shown little interest in establishing a framework of rules to cover all types of labour flows associated with or required for the cross-border provision of services. In contrast, developing countries, especially the net labour exporters, appear more enthusiastic to reach an agreement with developed countries that places the growing international trade in labour services within a multilateral framework.

There have been few studies on the impact and implications of trade in labour services for developing countries. Such studies are needed in order to clarify the diverse interests of developing countries and so to provide them with guidelines for negotiating an agreement on labour mobility related to cross-border services trade.

This paper examines the experience with labour services trade of one small group of developing countries, namely the six member States of the Association of South-East Asian Nations (ASEAN). This group includes both net labour importers (Brunei and Singapore) and net

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labour exporters (Malaysia, Indonesia, the Philippines, and Thailand). As these countries have both common and divergent interests in the international trade in labour services, an analysis of their experience would be useful for an understanding of the complex set of issues associated with labour mobility and labour exports.

The paper begins with an examination of trends in labour flows in the six ASEAN countries. It looks at the size and economic impact of both skilled and unskilled labour flows within the region as well as from the region to other parts of the world. It then analyses the barriers to labour flows within and outside the region, and the potential for labour exports to developed countries by ASEAN countries. Finally, the paper suggests ways in which ASEAN countries, known for their moderating voice on many divisive issues in international fora, can play a part in narrowing the large differences between developed and developing countries on the need to liberalize international transactions in labour services.

I. LABOUR EXPORTS AND IMPORTS OF ASEAN COUNTRIES

Information on the volume, characteristics and economic contribution of services trade and labour flows in the ASEAN countries is sparse and often unreliable. One source is the balance-of-payments data compiled by the International Monetary Fund (IMF). In 1987-88, Indonesia, the Philippines and Thailand registered overall balance-of-payments deficits, while Singapore and Malaysia enjoyed surpluses. Were it not for its net positive earnings from labour exports, the Philippines' balance-of-payments deficits in 1987-88 would have been much larger.

The limits of the reliability of the statistics is demonstrated by the fact that only Indonesia and Singapore have no entries for either exports or imports of labour services. This does not mean that they do not export and import labour services, but rather that earnings from their trade in labour services are classified differently. Labour services earnings can be reported in two ways. They can be classified as labour income, which includes wages, salaries and other compensation earned by persons in another country or as worker remittances. Work carried

out by nationals abroad can can also be included among payments for 'other services'. The distinction between individuals whose earnings are classified as labour income (persons who are not residents of the country where they work) and migrants (persons who have become residents of that country) is hard to draw in practice.

There are no data for Brunei, the sixth member of ASEAN, but other evidence suggests it is a heavy net importer of labour. Only the Philippines have entries for both exports and imports of labour services, while for Malaysia only export data are available. Thailand is, surprisingly, a net importer of labour services, but this may be because Thailand's considerable income (estimated at about $800 million a year in the late 1980s) from labour exports was not included in the column on labour services earnings.

Exports of labour services from Malaysia constitute about a quarter of the country's total service exports in 1988. The ratio is about one-fifth in the Philippines. Because IMF data on labour services earnings are incomplete and imperfect, the picture they reveal of ASEAN countries' trade in labour services leaves much to be desired. Other sources are needed to form a fuller impression of the pattern of labour services trade in ASEAN countries.

Table 1 shows the annual outflow of contract workers from three ASEAN countries. It suggests the outflow was growing fastest in the early 1980s and has slowed since then. In 1979-89, the average annual growth rate of the outflow of Filipino contract workers was 14.3 per cent. As table 2 suggests, remittances by Filipino and Thai workers have been substantial, averaging over $800 million a year in recent years. Though table 2 does not show it, Malaysia also earns considerable foreign exchange from its export of workers, especially to Singapore.

As data from international agencies provide at best a partial picture of ASEAN labour flows, we must turn to individual-country data. But country data too have their limitations. For one thing, they are often not consistent or up-to-date. Second, they do not cover with equal reliability or comprehensiveness all types of labour flows. And third, they are typically deficient on the economic dimensions of labour flows.

1. Brunei

In 1988, Brunei Darussalam had an estimated 36,000 foreign workers of whom 32,000 were employed in the private sector. Among ASEAN countries, it has the largest ratio (41 per cent) of foreign workers to the domestic workforce. In the private sector, 71.1 per cent of the workers are foreigners. Brunei's high dependence on foreign labour is likely to deepen in the future because of its small population and planned economic diversification and infrastructure development.

2. Indonesia

Historically, Indonesia has not been a major exporter of labour services. In colonial times, its main labour export consisted of the supply of workers for Dutch shipping lines. Since then, Indonesia's labour exports have grown, but they remain small compared to those of Thailand or the Philippines. Indonesia exported few workers in the 1970s and early 1980s. Table 3 shows that Indonesian labour exports have increased from an average of about 20,000 a year in the early 1980s to an average of 55,000 a year in the late 1980s. The country composition of the outflow has changed too. The Middle East, particularly Saudi Arabia, replaced the Netherlands in the 1980s as the major importer of Indonesian labour. Most of the Indonesians in the Middle East are employed in personal services occupations. Malaysia and Singapore are also major importers of Indonesian labour. A few developed countries - notably, the United States and Japan - have also imported Indonesian workers. It is not clear from the statistics what occupational activities these workers are engaged in. Table 3 reports only approved Indonesian workers abroad and does not include the large number of undocumented Indonesians who are working in Malaysia. Most Indonesian migrant workers are found in domestic services, which explains the high proportion (65 per cent) of women among Indonesian migrant workers. Male migrant workers are mainly in shipping and agriculture.

There is little information on remittances of Indonesians working abroad. Like some countries, Indonesia requires its citizens working

abroad to remit a minimum percentage (50 per cent) of their earnings through banking channels, but this requirement is apparently not strictly enforced. Figures from the Bank of Indonesia suggest that remittances by Indonesian migrant workers reached its peak in 1985. Since then, they have fallen, mainly because fewer Indonesians are working in the Middle East. It is likely that remittances from Singapore and Malaysia where a growing number of Indonesians are working have risen, but this rise is not reflected in table 5.

3. Malaysia

Malaysia is both an exporter and importer of labour services. It has a large number of foreign contract workers - approved as well as undocumented - in its construction sector and in its labour-short rubber and oil palm plantations. In addition, it has growing skill shortages, especially in manufacturing. At the same time, it is a major exporter of skilled and unskilled labour to Singapore.

Malaysia, like Singapore, issues employment passes to approved foreign managerial, professional, supervisory, technical and skilled workers. The number of high-earning foreign workers fell in the mid-1980s when Malaysia hit a bad economic patch. Since 1987, with the large influx of East and South-East Asian investments, the number has probably risen. Six destinations account for a large share of the employment passes issued: they are Japan, Singapore, Republic of Korea, Taiwan Province of China, the United States and United Kingdom, all countries with considerable or growing investments in Malaysia.

There are also large numbers of foreign workers in the East Malaysian state of Sabah. In 1988, foreign workers outnumbered citizen workers in Sabah by a ratio of two to one, and they form the majority of the workers in several sectors including agriculture and services (table 6). In oil palm and cocoa plantations, 90 per cent of the workforce are foreigners.

In contrast to Sabah, Sarawak, another East Malaysian state, has relatively few foreign workers. In the early 1980s, about 2,000 em-

ployment passes a year were issued to foreigners, half of them to workers from the Republic of Korea and Taiwan Province. Professional foreign workers came mostly from the developed countries but foreign construction workers were provided mainly by Korean construction firms.

There are no time-series data on earnings remitted by foreigners working in Malaysia. One estimate by the Manpower Ministry puts the amount of funds repatriated by foreign workers at $137 million in 1989. This amount is less than the $200 million remitted by the estimated 100,000 Malaysians working in Singapore and elsewhere.[1]

4. The Philippines

The Philippines has long been a large supplier of labour to foreign countries. In the nineteenth century, Filipino workers were employed in Hawaii, Guam and Alaska.[2] Since the 1950s, labour exports from the Philippines have diversified greatly in terms of skill and destination. There are Filipino workers in many Asian countries, in the Middle East and in OECD countries. The Middle East was a major importer of Filipino contract workers in the 1970s, and it continued in the 1980s to be reliant to Filipino labour, though at a declining rate. There are also large numbers of Filipinos employed as domestics or construction workers in several Asian economies including Hong Kong and Singapore. More recently, there has been a flow of skilled technical and professional Filipino workers into the fast-industrializing Malaysia and Thailand.

In the 1970s and early 1980s, Filipino contract workers increased rapidly.[3] In 1981, about a quarter million Filipino contract workers went abroad, mostly to the Middle East. Saudi Arabia was the largest absorber of Filipino contract workers. Except in 1985-86, Filipino

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1 Pang Eng Fong, "Foreign Workers in Singapore: Recent Trends and Policies", paper presented at the Workshop of Gastarbeiters in ASEAN, Singapore, December 1989, p. 11.

2 Charles W. Stahl, "Manpower Export and Economic Development: Evidence from the Philippines", *International Migration Review*, Vol. 26.

3 *Ibid.*, p. 3.

labour exports have continued to expand in the 1980s (table 7). In 1989, the Philippine Overseas Employment Administration processed over half a million workers, most of whom were able to find work abroad. About a third of the Filipinos employed abroad in the late 1980s are production workers. Another quarter are engaged in professional, technical and related work. Roughly the same proportion work in service occupations, mostly as domestics. Over half the migrant workers are men.

Remittances by Filipino workers abroad in 1980 were around \$815 million, equivalent to 14 per cent of commodity exports. In the first eight months of 1989, remittances were estimated at \$606 million, an increase of 6 per cent over the same period in 1988. These estimates leave out large amounts of funds sent back by Filipino contract workers by other means, e.g. couriers. Remittances through normal banking channels probably account for no more than half the total remittances.

5. Singapore

Rapid industrialization since the late 1960s has made Singapore increasingly dependent on foreign labour, both skilled and unskilled. In 1970, there were about 73,000 foreign workers in Singapore. By 1980, the number had risen to nearly 120,000, which formed 11 per cent of the workforce. In 1988, there were an estimated 157,000 foreigners in Singapore's workforce.[4] Foreign workers are over-represented at the top and bottom ends of the skill ladder in Singapore. There is a great shortage of lower-skilled workers, particularly in manufacturing and construction as well as increasingly in services. As Singapore upgrades its economy and attracts more skill-intensive investments, its need for highly-trained and experienced manpower, of which there is already a shortage, will grow. Despite great efforts to expand local supply, it will have to import more skilled foreign workers to sustain its development into a high-tech service and manufacturing economy.

As a result of investments in infrastructure and training, Singapore is also increasingly competitive in many traded services, in-

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4 Pang, *op. cit.*, p. 10.

cluding air and sea transport, banking, professional and business services, and software services. Many Singapore-based firms have secured overseas projects including a few in developed countries and have engaged skilled professionals from Singapore and elsewhere to work on these projects. Though official numbers are not available, it is likely that there are at least several thousand workers engaged on overseas projects won by Singapore-based firms.

6. Thailand

Historically, Thailand has not been a major exporter of labour services. But since the 1970s when it began encouraging labour exports, it has developed into a large exporter of labour, mainly to the Gulf countries. More recently, it has sent thousands of construction workers to Singapore. According to Stahl, there were less than 4,000 migrant workers in 1977.[5] By the early 1980s, this number had risen sharply to over 40,000, mainly because of labour demand in the Middle East, particularly Saudi Arabia, which absorbed over 75 per cent of all Thai labour migrants.

Since the early 1980s, labour demand in the Middle East has weakened and that in East Asian countries expanded. As a result, Thai labour exports have diversified. The proportion of Thai migrant workers in Asia, particularly in Singapore, Brunei, and more recently Japan, has risen rapidly in the late 1980s. As table 9 shows, the ASEAN countries accounted for about 11 per cent of all Thai labour exports in 1988 compared to less than 1 per cent in 1980. In 1988, there were some 4,000 Thai workers in Europe and the United States, but it is not known what sort of projects they were engaged in.

With the rapid growth of labour exports, remittances via normal banking channels have increased greatly from about $500 million a year in th early 1980s to around $1 billion in the late 1980s. These remittances have improved Thailand's balance-of-payments position, but they have not been as critical to Thailand's rapidly growing economy

5 Charles W. Stahl, "International Labour Migration and the ASEAN Economies", *ASEAN-Australia Working Papers*, No. 1, p. 13.

as they are to the Philippine economy, which has been less successful than Thailand in expanding manufacturing exports in recent years.

II. EMERGING PATTERNS OF LABOUR MOBILITY IN ASEAN

As a group, ASEAN countries are net exporters of labour services. Most temporary ASEAN migrants have been employed in the Middle East. But in the last few years, there has been a significant shift in the pattern of labour migration away from the Middle East which has been experiencing economic difficulties to the rapidly-integrating and growing East and South-East Asian economies. There has also been some increase in the export of temporary labour to developed countries, particularly Japan.

This emerging pattern of labour migration involves both approved contract labour as well as undocumented workers. While the growing intra-regional labour flows have alleviated shortages in the importing countries, they have also created new problems which threaten to strain relations between labour-exporting and labour-importing countries. They have called attention also to the need for clear rules and regulations on cross-border labour mobility.

The intra-regional Asian labour migration involves large numbers of unskilled workers responding individually to new opportunities in labour-short economies, as well as skilled and unskilled labour moving temporarily as an integral part of the cross-border provision of services such as construction and engineering. Both types of labour flows are likely to grow in the future, even though some of the labour pressure will be reduced by the relocation of manufacturing firms from labour-short to labour-surplus economies. This is because labour-short economies like Japan, Taiwan and Singapore are experiencing shortages in many non-manufacturing sectors including personal services, construction, tourism, where offshore production is not possible or feasible.

III. REGULATORY AND NON-REGULATORY BARRIERS TO LABOUR MOBILITY

For a variety of reasons - public order, security, public health, protection of local employment, etc. - all countries have national laws and measures that restrict the cross-border movement of labour. They stipulate conditions for entry into their territory and specify, usually in great detail though not always in a transparent manner, regulations covering such matters as issue of entry permits, visas, residence and temporary work permits. They also set conditions relating to the right of approved foreigners to pursue a particular profession or activity.

In addition to these nationally-set conditions, there are bilateral, regional and international arrangements and instruments regarding the national control of aliens to facilitate the international movement of labour. A bilateral economic pact between Australia and New Zealand, for example, allows for the free flow of labour between the two countries. An example involving a region is an agreement among the five Nordic countries to let labour flow freely within the Nordic region. There is already free flow of labour within the European Community (EC). With EC-1992, the harmonization of rules and regulations relating to the mutual recognition of professional qualifications and competence among member countries will be speeded up.

An important and instructive example of a bilateral agreement that contains provisions on the movement of persons is the Canada-United States Free Trade Agreement. The Agreement is intended to facilitate the temporary entry of persons on a reciprocal basis. It establishes transparent criteria and procedures while ensuring border security and permanent employment. The two parties - Canada and the United States - will authorize temporary entry of four groups of business people (business visitors, traders and investors, professionals and the employees of multinationals), subject to conditions relating to public health and safety and national security. The occupations and professions enjoying special facilities are spelt out in detail in two lists. The parties agreed also to exchange information and to publish their regulations.

Internationally, there is an ILO Convention concerning Migration for Employment, ratified so far by only fifteen member countries, which sets out in general terms conditions and rules for specified types of labour migrants. Within the ASEAN region, there are no bilateral or multilateral agreements allowing for the unrestricted flow of migrant labour among signatory countries. Although the ASEAN group does not have a regional agreement on migration for employment, its member states have agreed to visa-free, short-term, non-employment-related entry for ASEAN nationals. This visa-free arrangement for travel by ASEAN nationals within the region has greatly encouraged regional tourism and business.

1. Brunei

Like the other ASEAN countries, Brunei has rules and regulations relating to the temporary entry of foreigners into its territory, and stipulates conditions for foreigners who want to practise in a particular profession or activity. The recruitment of foreign workers is the joint responsibility of the Ministry of Home Affairs and its Departments of Labour and Immigration. The Immigration Department issues various classes of work permits and employment passes in consultation with the Labour Department. There is no legislation stipulating the sources of foreign labour. But the Government discourages the recruitment of foreign workers from distant lands by requiring employers to pay larger deposits. Workers from ASEAN countries pay a deposit of B$600, but those from the Asian subcontinent or Japan pay B$1,800. To facilitate the recruitment of ASEAN nationals, Brunei's diplomatic missions in the ASEAN capitals are allowed to issue work permits to approved ASEAN workers.

2. Indonesia

There are complex rules and restrictions governing the conditions of entry of foreign professionals who want to work in Indonesia. In general, these rules and restrictions are designed to ensure that firms do not depend too heavily on expatriate labour. Firms employing

expatriate workers must have approved plans to train Indonesians who will eventually replace the expatriate workers. Work permits issued to foreign workers may be for a year or for a short period, in order to allow for irregular visits by an expatriate working in Indonesia. Indonesia has a list of occupations which are closed to foreigners. Like the other ASEAN countries, it does not have a clear-cut policy on the export of critical skills.

Procedures for the recruitment of Indonesian labour for overseas projects are complicated. Two directorates within the Department of Manpower and Transmigration regulate and supervise labour recruitment: the Sub-Directorate for Inter-regional and Overseas Employment helps licensed agencies to recruit workers, while the Directorate General of Manpower Protection approves contracts lodged with the Sub-Directorate. There are over 60 licensed recruitment agencies, of which about 40 are authorized to send workers to Saudi Arabia, the major importer of Indonesian migrant labour. No legal minimum wages or recruitment fees are set, but the process of recruiting Indonesian workers for overseas can be time-consuming. Firms that want to hire Indonesians must fill out a job order form giving particulars of firms, the type and number of workers they require, and the terms of employment. The Indonesian Embassy of the country where the workers will be employed must verify these documents before forwarding them to the firm's Indonesian representative.

The representative may then formally request the desired number of workers from the Department of Manpower and Transmigration, giving details on the purpose of the recruitment and the transport his firm is providing for the workers. The Department of Manpower and Transmigration either contacts local employment offices to fill the contracts or carries out open registration, requesting employers or their representatives to make the final selection. The Department of Manpower and Transmigration is responsible for verifying the employment contract.

3. Malaysia

Like the other ASEAN countries, Malaysia has elaborate rules on the temporary entry and employment of foreigners. It requires all non-citizens living and working in Malaysia to obtain work permits. An employment pass must be obtained for the following types of employment: employment in a factory or business establishment, the installation of machinery and other equipment, and employment in a government or quasi-government body or in the private sector. A Visit Pass (Employment) is issued to any person with a contract of employment of less than two years and who is paid a salary of not less than M$1,200 a month.

Malaysia allows foreign companies to bring in expatriate workers in areas where they cannot find qualified local workers. But it does not, unlike some countries, require foreign firms to have only local personnel after a number of years of operations. Foreign firms with more than half a million dollars of foreign equity participation are allowed to fill certain "key posts" permanently with foreigners. For executive posts which require professional qualifications, expatriates may be employed for a maximum period of ten years.

Unlike some ASEAN countries, Malaysia does not actively encourage labour exports. But it does have legislation regulating the recruitment of Malaysian labour by private employment agencies. The Private Employment Agencies Act 246, 1981 requires such agencies to provide the Director-General of Manpower with particulars of prospective employers, the number of workers they need, the terms and conditions of employment, etc.

4. The Philippines

As already noted, the Philippines is a large exporter of skilled and unskilled labour. In order to facilitate labour exports, and to protect workers and their families, it has developed an elaborate institutional framework for administering and regulating labour recruitment. Before 1982, it had three bodies responsible for regulating labour recruitment

of labour while the Overseas Employment Development Board (OEDB) recruited workers for overseas employment. The OEDB supplied labour on a government-to-government basis, leaving private agents to handle other overseas employers individually. The third body, the National Seamen's Board (NSB) handled the recruitment of Filipino seamen. In 1982, the three bodies were merged to form the Philippine Overseas Employment Authority (POEA).

The POEA has three offices: a market development office, a licensing and regulation office, and a worker assistance and adjudication office. Its administrative innovations include: an Airport Labour Assistance Centre, a Regional Labour Centre for the Middle East and Africa based in Riyadh, a Worker Centre in Singapore and Hong Kong. It also provides assistance to foreign governments that want to recruit Filipino labour, but its policy is not to compete with private sector agencies.

Recruitment of Filipino labour for overseas work may begin only after the local recruitment agency has submitted documents from a potential employer and obtained approval from the POEA. After approval, the employer is accredited to the local recruiter. Accreditation is valid for one year. The agency and employer are jointly held responsible for the latter's breach of contract. Recruitment agencies must conduct pre-departure orientation for workers leaving to take up overseas employment. The POEA's airport assistance centre issues a clearance stamp to workers who possess machine-validated travel exit passes and notices of employment. Like the other ASEAN countries, the Philippines allows firms to hire foreign workers who possess skills not available locally. However, it has rules requiring these firms to train local understudies to replace these workers within an approved period.

5. Singapore

In contrast to the Philippines, Singapore is a major importer of both skilled and unskilled labour. It issues two types of immigration passes, namely, professional and employment passes and work permits. Employment passes, usually valid for the duration of the foreigner's employment contract in Singapore, are issued to skilled, technical,

managerial and professional workers. Work permits are issued to unskilled workers. For immigration purposes, unskilled workers are defined in terms of salary. Unlike some countries which have drawn up lists of skilled and unskilled occupations and regulate the entry of foreigners accordingly, Singapore uses a simple, easily understood criterion. Foreign workers who are paid a salary above a minimum (S$1,500 a month in 1990) are issued employment passes, while those earning less than the stipulated minimum are given work permits. Employment pass holders may bring with them their immediate family members, but work permit holders may not. The employers of the former do not have to pay a levy while those who employ work permit holders must. The levy raises the cost of hiring unskilled foreign workers, the importation of which Singapore discourages, but cannot do without because of its small domestic workforce and strong labour demand.

Visiting professional workers (entertainers, architects, lawyers, accountants, consultants, journalists) coming to Singapore to carry out approved contracts or assignments are given temporary professional visit passes. Singapore also issues block work permits allowing employers to bring in an approved number of workers for construction projects. In the 1980s, Singapore like other labour-short countries, attracted many undocumented and illegal workers from Asian countries. Stiff penalties are incurred both by foreigners convicted of over-staying 90 days or more in Singapore, and by employers convicted of knowingly hiring five or more illegal workers. There are also a large number of Singaporeans who work abroad, many on projects in developed countries. It is not known whether they encounter any difficulty in obtaining permits to work in these countries.

6. Thailand

Like the other ASEAN countries, Thailand has elaborate rules governing the entry of foreigners who want to work in Thailand. It closes many occupations to foreigners. These include not only manual occupations but also some professional occupations including engineering, accounting, architecture and law. Foreigners working on con-

tracts for the government or employed by companies that enjoy investment incentives approved by the Board of Investment have little difficulty in obtaining work permits.

Like the Philippines, Thailand has an active employment programme promoting the export of Thai workers. The Overseas Employment Administration Office (OEAO), which is in charge of this programme, maintains a manpower registry that private recruiters can consult. The recruitment of contract workers, however, is highly decentralized, and largely carried out by unregistered agencies. The Department of Labour estimates that 20-30 per cent of overseas contract workers coming are hired through registered licensed firms who are allowed to recruit workers for a service charge equivalent to 25 per cent of the worker's first month's salary.

For licence-holders recruiting labour for overseas work, the supervising authority is the Overseas Employment Service Division of the Department of Labour, under the Ministry of Interior. The latter has established guidelines and regulations regarding workers abroad, and it scrutinizes employment contracts before licence-holders can go about recruiting workers. The recruiting agencies are responsible for obtaining passports and visas for the workers. They do not need, unlike agencies in the Philippines, to post security bonds to guarantee the repatriation of workers in the event of contract violations.

IV. LABOUR MOBILITY AND SERVICE EXPORT POTENTIAL OF ASEAN COUNTRIES

The regulatory barriers ASEAN countries have erected to control the movement of people reflect national concerns and interests. Most of the barriers are not designed specifically to obstruct the cross-border provision of services. The growing need for foreign investment and expertise in recent years has made ASEAN countries more aware of the importance of clear rules on the entry of foreign firms and workers. As a consequence, there are growing efforts to streamline and even liberalize rules for the granting of visas, entry and residence permits to foreigners. To reduce irregularities and abuses, labour-exporting ASEAN countries have strengthened efforts to regulate the export of

labour services. Such efforts will help improve relations between themselves and importing countries.

As a group, ASEAN is a labour exporter, particularly of low-skilled labour. A high but falling proportion of this migrant labour goes to the Middle East. The current instability in the Gulf region is likely to accelerate this declining trend, and reduce sharply the foreign exchange earnings of ASEAN countries from unskilled labour exports.

In contrast, the importation of unskilled ASEAN labour by Asian countries, including several ASEAN members, is rising rapidly. This increase has benefited economically both labour importers and exporters, but it has also focused also attention on the need for rules to prevent abuses of legal migrant workers and to penalize the employment of illegal workers.

Thanks to rapid economic progress, ASEAN countries are increasingly reliant on skilled and professional foreign workers from the Asian region as well as from the developed countries. Both ASEAN and developed countries therefore have a shared interest in ensuring that the international flow of skilled workers is not impeded by unnecessary or cumbersome regulations.

ASEAN countries are net importers of skilled labour from developed countries. If they liberalize service sectors such as telecommunications, banking and insurance, construction and engineering services, professional services, transportation services, and tourism services, they may accept commitments to admit more skilled workers from developed countries. To the extent that such skills can be effectively transmitted to nationals, their economies will benefit from this increased inflow of skilled workers.

ASEAN's participation in world trade is growing along with its net exports of unskilled labour and net imports of skilled labour. If trade in services is liberalized, ASEAN's potential as an exporter of both skilled and unskilled labour will expand. Much of this expansion will be to the fast-growing countries within the region, but there exists also a potential for exports of skilled and unskilled labour to developed countries as well as the emerging market economies of Eastern Europe.

Table 10 estimates the potential for the export of skilled and unskilled labour from ASEAN countries to developed countries in the 1990s in the six sectors included in the Group of Negotiations on Services. It is based on a subjective evaluation of the comparative advantage of each ASEAN country in the six sectors. In telecommunications, only Singapore appears to have some potential for exporting skilled labour to developed countries. The other countries lag behind Singapore in telecommunications development and manpower. In construction services, the four larger ASEAN countries have a competitive edge in the export of construction services requiring large numbers of unskilled workers. If developed countries open their construction markets, firms from these four countries will be able to win contracts, provided they can bring with them labour from their countries. Singapore, in contrast, has acquired a capacity to export construction and design services that require skilled labour as a mode of delivery. Its export of construction services has gone mostly to Asian countries. If there is easier access to developed country markets, Singapore will be able to diversify geographically the markets for its construction services.

Transportation is another area in which many ASEAN countries already have a competitive edge. ASEAN countries have achieved or are fast developing a competitive capacity in air transport services.[6] If there is increased access to developed country markets, their export of transportation services will expand. This expansion will be reinforced if the skilled and unskilled personnel involved in the delivery of these services are able to enter developed countries on a temporary basis without undue hindrances.

There is some potential also for ASEAN exports to developed countries of tourism services that require labour mobility as a mode of delivery. This potential will be more quickly exploited if ASEAN workers, skilled and unskilled, can obtain easily temporary entry into developed countries to deliver tourism services.

Three countries - Malaysia, Philippines and Singapore - have the skilled manpower to deliver financial services in developed countries.

6 See Christopher Findlay and Peter Forsyth, "ASEAN Interests in Air Transport Services in the Uruguay Round", elsewhere in this volume.

Singapore, in particular, is in a good position to compete in providing financial services in a few market niches in developed countries.

In professional services, a sector where labour mobility in many instances is the only mode of delivery, there are good prospects for ASEAN exports to developed countries. The Philippines, with its large stock of skilled manpower, can become competitive in a variety of software and computer services. Singapore, which has made great efforts to develop an information technology industry, has firms that could compete in developed countries. Malaysia, Indonesia and Thailand have the capacity to establish a competitive advantage in some types of professional services in the medium term.

In the short term, ASEAN countries - potentially a very competitive group of developing countries in traded services - will not gain much from the liberalization of rules on the temporary entry of foreign workers if this liberalization is confined only to skilled or essential personnel needed for delivering a specific service. In the longer term, however, they stand to gain from liberalized rules on labour mobility, especially if the types of labour that are granted easier access to developed countries are not narrowly defined. In the North-South context of negotiations on trade in services, it is in the interest of ASEAN countries (and other developing countries) to seek an agreement that recognizes the broad range of skills which enable them to be competitive in particular services.

V. ASEAN AND THE GNS NEGOTIATIONS ON LABOUR MOBILITY

Both the ASEAN countries and the developed countries can facilitate labour mobility by making more transparent their national laws and regulations relating to the entry and employment of foreign workers. There is a need for greater transparency in regulations on the recognition of qualifications and the standards of practice in a particular profession and activity. Within the ASEAN region, little headway has been made towards the mutual recognition of qualifications and competences. But progress is more likely when rules on immigration and acceptance of qualifications for entry into a profession or activity are

clearly established and known. Increased intra-ASEAN flow of services would also strengthen the demand by professional organizations within the region for government initiative to facilitate the mutual recognition of professional qualifications. Such recognition would strengthen the group's negotiating position for easier entry by its workers into developed countries.

Although progressive liberalization is an objective of the Uruguay Round negotiations, they also need to take account of the level of development of individual countries. In the case of labour mobility, access concessions could involve liberalization of the mode of delivery for certain sectors or sub-sectors. Such concessions would not infringe on their sovereignty in immigration-policy matters and would respect national objectives of public order, safety, health and security.

For the ASEAN countries as well as developed countries, a framework for trade in services must deal with different types of labour mobility. It is important, for example, to distinguish between labour mobility that is crucial if the service provider is to carry out his contract or maintain his competitive edge, and labour mobility that is not time-constrained or tied to a specific project. The first type of labour mobility is less problematic, but the second raises, for ASEAN as well as for other countries, issues that go beyond the cross-border provision of services.

As indicated above, labour movement concessions can be and have been extended on a bilateral or even regional basis. The ASEAN agreement on visa-free, non-employment-related entry by ASEAN nationals is an example of non-discrimination on a regional basis. It appears that the Framework would permit preferential agreements of this nature among developing countries. ASEAN countries could seek concessions from developed countries in certain sectors, for example from the European Community or the Nordic States in order to facilitate travel by business people.

In the future, it is possible that ASEAN countries will negotiate a set of rules regarding the issue of visas and permits to foreign service suppliers that need to bring in staff for their projects. As similar rules are developed by other regions, there will be a potential for reciprocity

arrangements which would facilitate the cross-border provision of services. An agreement facilitating the temporary entry of workers employed by service suppliers into liberalized service sectors could initially be restricted to specified occupations and service sectors, as in the case of the United States-Canada Free Trade Agreement, and later extended to cover other occupations.

The principle of national treatment when applied to labour mobility raises many issues. What sort of administrative practices and regulations should apply to foreign service suppliers? How should foreigners be treated relative to nationals, for example, with respect to working conditions, pay, social security treatment, etc.? In the ASEAN countries, practices vary greatly, depending on the issue. In Singapore, for example, work-permit holders used to contribute to the Central Provident Fund, a compulsory savings scheme to which both employers and employees make contributions, but they are not required to joine the scheme since the introduction of a levy on work-permit holders.

It is important finally to bear in mind that trade in labour services, as with trade in other goods, benefits all participants, though not necessarily equally. The more definite and transparent the negotiated rules are on temporary labour mobility and on the recognition of professional qualifications, the greater is the likelihood that the time-limited and project-related flow of personnel to provide cross-border services will not develop into immigration problems for the importing country. Indeed, clear rules facilitating temporary entry by personnel providing cross-border services in service sectors that are granted market access can help reduce the flow of would-be migrants from developing countries to developed countries.

Box 1

LABOUR MOVEMENT IN THE URUGUAY ROUND CONTEXT

Since the initiation of the debate leading up to the negotiations of a multilateral framework for trade in services in the Uruguay Round, developed-country negotiators have been insisting that, for a large number of service sectors, access to foreign markets would require movement of capital in the form of establishment or at least "commercial presence" in the importing market. Developing countries have taken the position that if the multilateral framework were to provide for the liberalization of capital flows, it would have also to include "symmetrical" provisions with respect to the movement of labour. The rationale for such a position was quite clear - for many developing countries, exports of services were primarily accomplished through the "mode of delivery" of persons crossing international frontiers. Any multilateral regime which liberalized capital movement while continuing to restrict labour movement would, in effect, serve to transfer resources from the latter factor to the former.

In this context, the issue of symmetry also covered the temporal nature of the factor movement, i.e. that the framework should not envisage the "temporary" movement of labour while accepting the "permanent" movement of capital. For this reason, developing countries insisted on including, in the results of the Uruguay Round Mid-Term Review (Montreal, December 1988), provisions that the definitions of trade in services should cover cross-border movement of factors of production where such movement is essential to suppliers and where such movement involves (a) cross-border movement of service and payment, (b) specificity of purpose, (c) discreteness of transactions, and (d) limited duration. The same document also recognized that when market access was made available under the framework, foreign services may be supplied according to the preferred mode of delivery.

As negotiations proceeded, it was decided to include a Working Group on issues relating to labour mobility among the sectoral groups set up under the Group of Negotiations on Services (GNS) in order to discuss specificities which may need to be taken into account in the application of the general framework for trade in services, and to examine whether there would be a need for sectoral annotation for the sector. At the time when this document went to press, the Working Group had met three times (25-27 June, 3-4 September and 8-9 October 1990).

In order to focus attention on their interests in this group, several developing countries (Argentina, Colombia, Cuba, Egypt, India, Mexico, Pakistan and Peru) submitted a proposal for an Annex to the multilateral framework on "Temporary Movement of Services Personnel". The major thrust of the Annex is that the temporary movement of all categories of services personnel essential to the effective delivery of a service be covered by the framework agreement, and that nothing in the Annex was intended to affect immigration laws and regulations dealing with permanent residence, establishment or citizenship. The Annex endeavoured in particular to ensure that immigration regulation neither act as an unnecessary barrier to trade in services, nor nullify and impair the benefits expected under the framework. It foresees essentially two situations: (a) where a foreign firm needs to bring its own employees to the importing country to provide a service, and (b) where foreign personnel are recruited abroad to provide a specific service. It clearly excludes cases of persons travelling to another country to seek employment.

Box 1 (continued)

LABOUR MOVEMENT IN THE URUGUAY ROUND CONTEXT

On the other hand, developed countries' proposals recognize the need for a certain movement of personnel, but oppose the inclusion of unskilled labour in the framework agreement and consider that capital and labour are different in nature and therefore need not be treated in a symmetrical manner. However, among these countries a difference exists in the approach of treating labour mobility in the framework. The United States has proposed an annex which indicates precisely the types of labour covered under the framework, essentially movement within corporate structures. Qualified employees of such firms are categorized into "managers", "executives" and "specialists", and maximum length of stay is specified as three to five years. The European Community has favoured dealing with the issue within specific market access committments along with other modes of delivery. It is foreseen that the country lists of concessions to be annexed to the multilateral framework would provide that specific reservations could be made with respect to four modes of delivery: (a) cross-border movement, (b) movement of consumers, (c) commercial presence, (d) movement of personnel with respect to those sectors or subsectors where market access would be conceded.

Box 2

REGULATIONS ON INTERNATIONAL MOBILITY OF SERVICE SUPPLIERS

There are a number of reasons why States may choose to liberalize the entry of foreign service providers such as workers, entrepreneurs, professionals, etc. These include the needs of the market, the pressures of the economy and international economic relations. While some of these entries may be by their nature temporary, other cases may involve entry for fixed duration or immigration. It has been observed that entries of fixed duration may correspond better in several cases with the need for entrepreneurship and flexibility, the need for manpower with specific qualifications and experience, and individual aspirations to greater mobility. In contrast with ordinary labour migration, entry of service providers for fixed duration may even create new employment possibilities within the host country.

The OECD Invisibles Code, the Capital Movements Code and the IME instrument concern the liberalization of cross-border trade in services, but they primarily address the movement of capital. Immigration policies and non-resident admission matters have traditionally been regarded as beyond the scope of these instruments. In OECD countries, there are regulations concerning visas as well as some professions that may relate to cross-border movement of persons. The former, primarily adopted for safeguarding public safety, health and security, may also be designed in order to ensure the employment of local labour and control over immigration. Regulations concerning professions may be intended to guarantee that certain professions are practised by persons with prescribed qualifications and other standards, or to prevent certain professions from being inundated or to restrict competition. Additional conditions relating to nationality or residence may also limit cross-border provision of services. The visa is the major travel document governing such temporary entry in most of the OECD countries. In Western Europe, since the 1950s, the need to have a passport to travel between European countries has progressively decreased, and passport has been replaced by the national identity card as the main travel document. The need for visas for intra-European travel has also lapsed, though not the need for residence or work permits. Bilateral agreements between some OECD countries have also eliminated the need for visas for short-stay business trips. Indefinite-term permits are possible, where the provision of services is through the permanent establishment of foreign companies, requiring long-term entry of manegerial or comparable personnel. The distinction between residence and work permits is increasingly disappearing, since both are often incorporated in a single document.

The Treaty of Rome, which founded the European Community, has provisions for the right of establishment of individuals and firms and for the freedom of movement of workers and service providers within the Community. Although the movement of persons from non-member States have been governed by the immigration laws of individual European countries, greater harmonization of Community policies on this issue is envisaged. Under the Common Nordic Labour Market - comprising Denmark, Finland, Norway and Sweden - nationals of member countries are permitted to work in other member countries without labour market tests or work permits. European Free Trade Association - comprising Austria, Finland, Iceland, Norway Sweden and Switzerland - allows the establishment of nationals of member States for the management of economic enterprises involved in the manufacture of *goods*.

In addition to the multilateral instruments mentioned above, there are a number of bilateral agreements between countries that have provisions concerning the cross-border movement of persons. The Canada-United States Free Trade Agreement provides for the temporary entry of four categories of business persons - namely, business visitors, traders and investors, professionals and employees of multinationals. There are provisions for equalization of qualifications for certain professions and for access to information on regulations. Under the Trans-Tasman Travel Agreement, Australians and New Zealanders are allowed to enter each other's country without visas or work permits. The 1988 Services Protocol provides for market access and national treatment to the service providers of the other country.

Box 2

REGULATIONS ON INTERNATIONAL MOBILITY OF SERVICE SUPPLIERS

Some developing countries are moving towards greater movement of labour on a subregional basis. For example, a 1980 protocol, ratified by the 16 member States of ECOWAS will, over 15 years, permit entry, residence and establishment of business by citizens of member countries in one another's territory. [a] Arrangements among ASEAN countries in this field has been discussed in the paper by Pang Eng Fong and Linda Low in this volume.

a For a discussion of co-operation on services among developing countries, see Luis Abugattas, "Services as an Element of Co-operation and Integration Among Developing Countries", in UNCTAD, *Trade in Services: Sectoral Issues* (United Nations Publication, UNCTAD/ITP/26), pp. 431-75.

Table 1

ANNUAL OUTFLOW OF CONTRACT MIGRANT WORKERS FROM THREE ASEAN COUNTRIES, 1969-89
(Thousands)

	Indonesia	*Philippines*	*Philippines* [a]	*Thailand*
1969	na	3.7	na	na
1970	na	1.9	na	na
1971	na	1.9	na	na
1972	na	14.4	na	na
1973	na	26.4	na	0.3
1974	na	32.7	na	na
1975	na	36.0	na	1.0
1976	1.9	47.8	na	1.3
1977	2.9	70.4	na	3.9
1978	8.2	88.2	na	14.7
1979	10.4	137.3	na	10.6
1980	16.2	214.6	na	21.5
1981	17.9	266.2	na	26.7
1982	21.1	314.3	na	108.5
1983	29.0	434.2	na	68.5
1984	37.9	425.1	351.0	75.0
1985	56.7	389.2	372.8	69.7
1986	69.5	414.5	378.2	85.7
1987	59.4	496.9	449.3	85.5
1988	64.0	477.8	471.0	118.6
1989	na	523.0	458.6	125.3

Source: Ministry of Labour in countries of origin, compiled in ILO/World Employment Programme, *Statistical Report, 1989*.

a Deployed Filipino migrant workers.

Table 2

REMITANCES BY MIGRANT WORKERS OF THREE ASEAN COUNTRIES, 1974-89
(million dollars)

	Indonesia	*Philippines*	*Thailand*
1974	na	118.0	13.0
1975	na	103.0	18.4
1976	na	111.0	23.8
1977	na	213.0	44.7
1978	na	290.9	103.8
1979	na	364.8	187.0
1980	na	421.3	365.0
1981	33.1	564.9	475.0
1982	47.9	810.5	618.0
1983	44.7	944.5	846.0
1984	52.7	658.9	894.0
1985	57.6	687.2	878.0
1986	39.2	680.4	789.0
1987	26.4	791.9	863.8
1988	21.6	856.8	936.5
1989	na	606.3	na

Source: Central Banks of countries of origin; data compiled in ILO/World Employment Programme, *Statistical Report, 1989*

Table 3

OUTFLOW OF INDONESIAN WORKERS BY COUNTRY OF DESTINATION, 1969-89

Country of destination	*1969-74*	*1974-79*	*1979-84*	*1985-89*
Australia	1	114	34	4
Brunei	0	0	0	762
Cyprus	0	0	67	0
Denmark	122	0	0	0
France	0	4	664	979
Greece	0	300	1,232	1,873
Hong Kong	144	1,297	1,761	1,670
Iran	0	935	0	0
Iraq	0	0	2,258	320
Italy	0	0	215	205
Japan	292	451	920	447
Jordan	0	0	179	27
Kuwait	0	0	1,210	783
Malaysia	12	536	11,441	36,205
Monaco	0	14	188	889
Netherlands	3,332	6,637	10,104	4,156
New Caledonia	1,189	10	0	0
Norway	0	0	50	35
Philippines	1	40	13	13
Saudi Arabia	0	3,817	55,976	219,015
Singapore	8	2,432	5,007	9,186
Sweden	0	23	0	0
Switzerland	0	75	41	0
Taiwan, Prov. of China	37	0	0	262
United Arab Emirages	0	0	470	1,012
United Kingdom	3	21	372	87
United States	146	176	2,981	3,029
West Germany	337	9	1,097	169
Other	0	151	130	309
Total	5,624	17,042	96,410	281,437

Source: Department of Manpower, Jakarta, Republic of Indonesia.

Table 4

DEPLOYED INDONESIAN MIGRANT WORKERS BY OCCUPATION, 1983-89

	1983	*1984*	*1985*	*1986*	*1987*	*1988*	*1989*
Agriculture	2,867	3,133	3,592	19,229	5,671	2,135	36,627
Mining	-	-	2	-	-	4	6
Industry	-	-	3	-	2	2	7
Electricity	-	361	195	-	2	36	594
Construction	312	1,313	1,396	342	154	216	3,733
Tr and Hotel	326	602	137	475	49	78	1,667
Con svcs	318	514	844	470	62	307	2,515
Dom svcs	12,630	21,638	42,224	36,808	43,108	50,001	206,409
Other	-	-	-	1	-	-	1
Total	28,957	37,857	56,696	65,544	59,362	63,998	312,414

Source: Department of Manpower, Jakarta, Republic of Indonesia.

Table 5

FOREIGN EXCHANGE TRANSFERS OF INDONESIAN OVERSEAS CONTRACT WORKERS, 1981-88
(thousand dollars)

Country	*1981*	*1982*	*1983*	*1984*	*1985*	*1986*	*1987*	*1988*
Bahrain	6	5	7	-	-	-	-	14
Iraq	101	960	320	17	-	-	-	-
Kuwait	827	429	496	202	1,472	210	156	26
Oman	5	4	-	-	5	-	-	-
Qatar	51	97	48	88	45	10	-	35
Saudi Arabia	30,522	44,270	41,595	49,926	52,941	37,333	24,662	20,591
Singapore	-	-	-	-	-	-	66	106
UAE	1,556	2,167	2,228	2,434	3,144	1,693	1,520	812
Yemen	1	-	19	-	-	-	-	-
Other	3	20	7	4	-	-	-	-
Total	33,071	47,952	44,720	52,672	57,606	39,245	26,404	21,585

Source: Bank of Indonesia.

Table 6

LOCAL AND FOREIGN WORKERS BY SECTOR IN SABAH IN 1988

Sector	*Local*	*Percentage*	*Foreign*	*Percentage*	*Total*
Agriculture	17,042	10.0	152,385	90.0	169,427
Forestry	30,557	53.0	27,098	47.0	57,655
Construction	10,979	50.7	10.690	49.3	21,669
Wholesale, retail, restaurants & hotels	41,821	71.6	16,582	28.4	58,403
Manufacturing	10,847	58.0	7,855	42.0	18.702
Services	30,892	32.8	63,253	67.2	94,144
Total	142,138	33.8	277,863	66.2	420,001

Source: Ho Ting Seng, "Economic Development and Guest Workers in Sabah", Paper presented at the Workshop of Gastarbeiters in ASEAN, Singapore, December 1989, p. 18.

Table 7

PROCESSED AND DEPLOYED FILIPINO CONTRACT WORKERS

	Number processed			Number deployed		
	Total	*Land*	*Sea*	*Total*	*Land*	*Sea*
1975	36,035	12,501	23,534	-	na	na
1976	47,835	19,221	28,614	-	na	na
1977	70,375	36,676	33,699	-	na	na
1978	88,241	50,961	37,280	-	na	na
1979	137,337	92,519	44,818	-	na	na
1980	214,590	157,394	57,196	-	na	na
1981	266,243	210,936	55,307	-	na	na
1982	314,284	250,115	64,169	-	na	na
1983	434,207	380,263	53,944	-	na	na
1984	425,081	371,065	54,016	350,982	300,378	50,604
1985	389,200	337,754	51,446	372,784	320,494	52,290
1986	414,461	357,687	56,774	378,214	323,517	54,697
1987	496,854	425,881	70,973	449,271	382,229	67,042
1988	477,764	381,892	95,872	471,030	385,117	85,913
1989	522,984	407,974	115,010	458,626	355,346	103,280

Source: Philippine Overseas Employment Administration.

Table 8

OCCUPATIONAL DISTRIBUTION OF PROCESSED FILIPINO MIGRANT WORKERS, 1975-1988

	1975	*1976*	*1977*	*1978*	*1979*	*1980*	*1981*
Prof/tech	4,670	2,924	2,650	5,238	9,584	11,966	12,347
Entertain	1,925	3,872	2,057	6,097	8,380	12,395	14,333
Mgr/admin	71	82	210	331	1,441	740	1,804
Clerical	225	370	944	1,516	2,896	5,383	2,585
Sales	53	16	30	69	265	451	446
Service	2,747	3,893	4,576	7,910	14,089	23,441	33,109
Agriculture	118	74	123	37	186	1,581	1,322
Prod	2,602	7,990	26,086	29,763	55,678	101,436	144,970
Total land	12,501	19,221	36,676	50,961	92,519	157,394	210,936
Total sea	23,534	28,614	33,699	37,280	44,818	57,196	55,307
Total	36,035	47,835	70,375	88,241	137,337	214,590	266,243

	1982	*1983*	*1984*	*1985*	*1986*	*1987*	*1988*
Prof/tech	15,010	39,814	51,403	57,617	60,753	112,236	na
Entertain	13,425	13,117	13,998	18,342	26,816	37,888	na
Mgr/admin	1,462	1,870	1,222	1,202	1,317	1,675	na
Clerical	8,519	14,189	15,117	15,141	15,261	15,929	na
Sales	1,394	2,259	2,295	2,780	3,562	4,268	na
Service	43,248	58,151	77,564	91,381	117,127	106,654	na
Agriculture	1,158	1,641	1,578	1,217	1,557	2,690	na
Prod	165,899	249,222	207,888	150,074	131,294	144,541	na
Total land	250,115	380,263	371,065	337,754	357,687	425,881	381,892
Total sea	64,169	53,944	54,016	51,446	56,774	70,973	95,872
Total	314,284	434,207	425,081	389,200	414,461	496,854	477,764
Deployed Filipino contract workers							
Total land			300,378	320,494	323,517	382,229	385,117
Total sea			50,604	52,290	54,697	67,042	85,913
Total			350,982	372,784	378,214	449,271	471,030

Source: Philippines Overseas Employment Administration.

Table 9

NUMBER OF THAI WORKERS ABROAD BY COUNTRY OF DESTINATION, 1977-88

Country	*1977*	*1980*	*1985*	*1986*	*1987*	*1988*
Middle East	3,831	20,690	61,659	85,659	78,094	78,518
Saudi Arabia	2,855	9,948	42,664	67,743	64,134	66,154
Iraq	-	959	6,101	8,116	4,434	2,756
Qatar	-	1,017	746	1,649	1,813	1,981
Bahrain	976	306	928	1,123	1,156	1,532
Kuwait	-	958	1,200	4,405	3,216	3,952
Africa	-	6,497	7,476	9,322	9,569	na
Libya	-	6,497	7,401	9,231	9,216	13,386
United States and Europe	-	-	-	1,518	2,598	4,133
ASEAN	-	191	7,494	11,001	10,443	13,442
Singapore	-	191	3,387	7,267	6,243	5,262
Brunei	-	-	2,160	2,596	3,300	6,792
Malaysia	-	-	1,861	1,138	884	1,238
Other Asia	-	-	452	2,119	4,138	8,151
Japan	-	-	359	na	1,367	3,942
Total [a]	3,831	27,378	69,655	112,443	105,988	118,957
Percentage distribution by region						
Middle East	100	99.09	88.52	76.18	73.68	66.01
Africa	-	-	0.06	8.29	9.03	12.37
United States and Europe	-	-	0.01	1.35	2.45	3.47
ASEAN	-	0.91	10.76	9.78	9.85	11.30
Other Asian	-	-	0.65	1.88	3.9	6.85
Total	100	100	100	100	100	100

Source: Ministry of Labour data cited in S. Khoman and V. Thosanguan, "An Economic Assessment of the Guest Worker Phenomenon in ASEAN: The Thai Perspective", Paper presented at the Workshop of Gastarbeiters in ASEAN organized by the Institute of Development Studies (Sabah), in Singapore, December 1989.

a Figures do not add up due to missing information.

Table 10

PROSPECTS FOR ASEAN LABOUR EXPORTS TO DEVELOPED COUNTRIES IN THE 1990S BY TRADED SERVICE SECTOR

Country	*Telecom.*		*Constr.*		*Transp.*		*Tourism*		*Fin.Ser.*		*Pro.Ser.*	
	Sk	*Unsk*	*Sk*	*Unsk*	*Sk*	*Unsk*	*Sk*	*Unsk*	*Sk*	*Unsk*	*Sk*	*Unsk*
Brunei	..	..	..	..	..	..	..	..	..	..	..	..
Indonesia	..	..	..	x	..	..	x	..	..	..	x	..
Malaysia	..	..	x	xx	x	..	x	..	x	..	x	..
Philippines	..	..	xx	xx	x	x	x	..	x	..	xx	x
Singapore	x	..	xx	..	xx	..	x	..	xx	..	xx	..
Thailand	..	..	x	x	x	..	x	..	..	..	x	..

Note:

..	Few opportunities
x	Some potential
xx	Good potential
Sk	Skilled labour
Unsk	Unskilled labour

TRADE IN INSURANCE IN KOREA

*Un Hoe Park**

INTRODUCTION

This paper attempts to assess some potential effects of trade liberalization in the insurance sector and to consider relevant policies for increasing the participation of Asian insurance firms in international markets. The paper addresses three issues in particular:

- Market structure and competitiveness;
- Regulatory and non-regulatory barriers to the export of services; and
- The possibility of increasing the competitiveness and expanding the international market of Asian insurance firms, including through the Uruguay Round negotiations on trade in services.

The study is based on experience in the insurance sector in the Republic of Korea for the past five years. However, data of other countries have also been used for comparative analysis.

Insurance trade can be classified into three different categories, according to the nationality of the parties concerned and to the territory in which such trade is conducted:

- Pure domestic trade between sellers and buyers of the same nationality in the same territory;
- International or across-the-border trade between sellers and buyers in two different countries; and

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- Domestic trade between local buyers with foreign business firms licensed to do business in that territory.

Each form of such trade can also be reclassified according to the nature of trade:

- Primary or direct insurance trade between the public and insurance companies;

- Reinsurance trade between or among insurance companies; and

- Other insurance-related trade done by agents, brokers, consultants, claims adjusters, etc.

Thus, trade in insurance can, technically speaking, take nine different forms. However, for the purpose of this study, "trade in insurance" in most cases will mean across-the-border trade of primary insurance and reinsurance, and commercial presence by the establishment of foreign insurance companies in the form of branch offices, subsidiaries, or by the establishment of joint-venture companies with equity participation.

According to an estimate made by *Sigma*, the size of the world insurance market in terms of premium income at current United States dollar value grew nearly 13 times in the period from 1967 to 1987. Asia has been the fastest-growing region, with a growth of over fifty times during this period. The Asian share in the world increased form 6.3 per cent in 1967 to 25.3 per cent in 1987.

The volume of Korean insurance market, in terms of premium, grew over 20 times from $550 million in 1977 to $11,142 million in 1987, showing the highest growth among 15 Asian countries. Its share in the Asian market increased from 1.4 per cent to 4.12 per cent during this period, and its ranking in the world also upgraded from 25th to 11th, the share increasing from 0.19 per cent to 1.04 per cent. During this period, the Korean economy grew only 3.5 times in terms of GNP, from $37 billion to $129 billion at current value. This implies that the growth of the insurance market was much higher than that of the national economy, the premium/GNP ratio moving from 1.5 per cent to 8.3 per cent in 10 years. The Korean insurance market can probably

be considered as a model for other developing countries with similar cultural and socio-economic backgrounds.

I. MARKET STRUCTURE AND COMPETITIVENESS

A. Economic background

Although the potential demand for insurance is limitless, effective demand is always limited by various factors such as the income of buyers, the cost of insurance from the viewpoint of consumers compared to other substitutes, the degree of social security, etc. However, one of the most significant factors that determine the demand for insurance is the level of economic development.

Korean economy has achieved a relatively high growth in the five years preceding 1988, with an average growth rate of 10.4 per cent in terms of real increase in GNP. The gross saving ratio, which is closely related to demand for life insurance, increased from 29.4 per cent in 1984 to 37.7 per cent in 1988, while the export of goods increased with an average rate of 21.5 per cent, reaching $59.7 billion in 1988. The exchange rate of Korean won to the United States dollar appreciated during this period by 17.3 per cent, though this trend has been reversed by a post-Olympics economic setback.

B. Legal framework

Insurance, in a broad sense, can include the government sector (social insurance, post-office, industrial, life and export-credit insurance) as well as the private sector (co-operatives insurance such as farmers, constructors, ship operators, taxi/bus/truck owners, and even teachers). However, these two broad sectors are entirely distinct from commercial insurance in terms of the legal framework as well as the supervising ministry. This paper will focus on the commercial insurance sector which is supervised by the Ministry of Finance in the Republic of Korea.

There are two basic laws regulating insurance trade in Korea: the commercial code is the private law stipulating the rights and obligations

of parties engaged in the contract of insurance, while the insurance business law as a public law is the basis of supervising insurance business entities. The insurance business law was first promulgated in 1962 and has been amended four times - in 1971, 1977, 1980 and 1988. This law is composed of the following nine chapters and addendum: General provisions, Insurer, Insurance solicitation, Insurance supervisory board, Insurance arbitration, Insurance guaranty fund, Insurance organizations, Supplementary provisions, and Penal provisions. The basic framework of this law, as relevant to this study, can be summarized as follows:

- Insurance companies must obtain permission from the Ministry of Finance to conduct business in Korea (article 5).
- Insurance companies must be joint-stock companies, mutual companies or foreign insurers (article 5).
- The minimum capital or foundation fund shall not be less than 10 billion won (approx. $14 million) for life, and 30 billion won (approx. $42 million) for non-life business (article 6).
- Insurers shall make a deposit with the Insurance Supervisory Board for the protection of its policyholders in an amount prescribed by Presidential Decree (article 6-2).
- No insurer shall operate life and non-life business concurrently except in the form of personal accident insurance (article 10).
- The Ministry of Finance may set limitations to the underwriting amount of direct insurance and retention in consideration of business scale, financial status, capacity and other conditions of the insurer (article 18).
- Foreign insurers shall hold in Korea the assets equivalent to liability reserve and contingency reserve (article 83).
- Insurance solicitors must register with the Insurance Supervisory Board (article 145).
- Insurance agents or brokers shall obtain permission from the Minister of Finance (article 149).

- Insurers shall contribute to the Guaranty Fund managed by the Insurance Supervisory Board, according to the amount specified in a Presidential Decree (article 197).

- Insurance Supervisory Board shall carry out such duties as the inspection of insurers, the management of guaranty fund and deposits, the registration of insurance solicitors, the registration of insurance actuaries and loss adjusters, and other business acting for or trusted by the government (article 179).

The Ministry of Finance and the Insurance Supervisory Board have specific organizational structures in order to enforce the legal framework.

C. Supply of insurance services

There are 48 insurance companies licensed to operate in Korea as of 30 June 1990. The number of insurance companies has drastically increased in the four years since 1987, as can be seen in table 1. This has been mainly due to political pressure by the United States demanding market access in order to offset its trade deficit in goods. While the negotiations between the Korean government and the United States Trade Representative were in progress, domestic pressure was also generated on the rationale that it was unfair to open the market only to foreigners as new entry had not been allowed even to Koreans for more than two decades. As the result, the Ministry of Finance, the regulatory authority on insurance, issued guidelines for new application in 1987, and issued licences to 27 companies during the period 1987-90. The number of life companies increased more than five times from 6 in 1986 to 32 in 1990, while the non-life companies increased from 15 to 16.

The ownership of insurance companies can be classified into three categories:

- 34 national companies, owned mostly by Koreans, with three exceptions in the case of non-life companies: Oriental Fire has 18.1 per cent equity participation of Royal (United Kingdom), Conti-

nental (United States) has 14.3 per cent share of First Fire, and Tokio Marine (Japan) has 12.9 per cent share of Koryo Fire.

- 6 Joint-venture companies, with a minimum of 49 per cent and a maximum of 60 per cent share owned by foreign companies: 5 from United States and 1 from Canada.

- 8 Foreign companies, including 6 branch offices and 2 locally registered subsidiaries, all owned by United States companies.

Thus, foreign participation in the Korean market is at present limited to only four developed countries: United States (12), Japan (1), United Kingdom (1), and Canada (1). See tabel 2.

The distribution of insurance products is largely handled by solicitors in Korea, particularly in the field of life business as seen in table 2. It is worth noting that over 95 per cent of life solicitors are female, mostly housewives. As in Japan, it has been believed that the most effective approach to selling life insurance is to employ housewives to contact housewives since they can meet one another easily, and since in most families in Korea, it is the housewives who take care of the daily expenditure.

In the field of non-life business, the practice is quite different, since the majority of the business (66.2 per cent) is produced in the commercial area rather than in households (33.8 per cent). The weight of agents has increased from 44.8 per cent in 1983 to 55.0 per cent in 1988, while the direct production by the company and pools have declined. Lines such as marine insurance, which requires professional skills, are in general handled directly by the company.

The total employment in the insurance sector is estimated to be over 360,000 persons as of March 1990, most of them engaged in distribution. The figures show an increase of 24 per cent in one year, particularly due to the establishment of new companies (table 2). The ratio of insurance employment in the economically active population is approximately 2 per cent, the figure for United States and Japan in 1983.[1]

1 J. Francois Outreville, "Trade in Insurances Services", in UNCTAD, *Trade in Services: Sectoral Issues* (United Nations Publication, UNCTAD/ITP/26), p. 182.

D. Premium structure

The total volume of premium income in the Korean insurance market has been growing at an average annual rate of 34.5 per cent in the period between 1985 and 1989 in current United States dollars. Such a high growth rate can be attributed to four main reasons:

- The national economy grew at an average real growth rate of 10.4 per cent in terms of GNP during this period.

- The exchange rate of Korean won to United States dollar appreciated from 827.4:1 in 1984 to 679.6:1 in 1989 - i.e. 17.9 per cent.

- Two government policies encouraged the public purchase of insurance: (a) premium payment up to won 240,000 (equivalent to United States $350) per year was made deductible from taxable income; and (b) insurance companies were allowed to charge a higher rate of interest for loans than banks, so that life insurance companies could maintain a comparative advantange over banks in the assumed rate of interest.

- The effectiveness - particularly in the life sector - of marketing strategies used by insurance companies, with their sales force of over 360,000 employees.

Within the sector, life insurance companies have achieved an average growth rate of 35.9 per cent compared to 29.6 per cent of the non-life field. Accordingly, the share of the life sector has increased from 77.9 per cent in 1984 to 81.8 per cent in 1989. This probably is the second highest share of life premium in a country, the highest share being in the case of South Africa (82.6 per cent in 1987).

Another peculiarity of the Korean insurance market concerns the high ratio of life premimum to GDP. This reached 8.34 per cent in 1989, which is even higher than Japan, the largest life market in the world (6.43 per cent in 1987). The ratio for non-life sector was 1.85 per cent, which is the level of many developing countries. Table 3 shows the correlation between GDP, per capita GNP, and insurance premium.

There have been changes in the composition of life premium in recent years. The weight of "pure endowment" has sharply increased, while other lines - particularly "against death" and "endowment" - have declined, mainly due to the increased demand for children's education and old-age pension. The structure of non-life business, on the other hand, showed relatively little change in recent years. Motor insurance has been the leading class, showing a constant increase due to the increased demand for motorization, while other conventional classes such as fire and marine have been losing their share, as in many developed countries.

A unique feature of the Korean non-life market is that the share of bond business (fidelity and surety) is exceptionally large compared to other countries, since bonds issued by insurance companies (though there are only two specialized companies), are generally accepted by most business firms and government agencies.

Long-term business is a kind of "homeowner's multiple peril" covering fire, accident, and other allied perils for a term of five to ten years. This product was introduced from Japan, and several companies are active in sales. However, this has not achieved the expected success, probably due to differences in attitudes between Japan and Korea. The weight of long-term business in Japan is reported to have reached nearly 40 per cent of the total non-life premium in 1989, as the protection-plus-saving structure of this product has been found attractive with respect to the Japanese consumer needs.

One weakness of the Korean non-life market is the declining share of casualty or miscellaneous class from 12.7 per cent in 1984 to 5.9 per cent 1989. The weight of primary insurance demand (fire, marine and motor) has further increased from 69.0 per cent in 1984 to 71.9 per cent in 1989.

E. Underwriting results

The underwriting results of life business in the last five years shows a decline in the share of the net premium in total income from 85.3 per cent in 1985 to 83.1 per cent in 1989, as investment income increased due to the accumulation of assets and to a higher yield in the investment in securities and real estate. Claims paid show some fluc-

tuation with an average of 51.7 per cent of the total income, while the net expense ratio has been decreasing due to economies of scale. There has been net profit after the accumulation of technical reserves in the last four years. This comes after four years of deficit since 1982, when drastic reduction in bank interest rates from 12 per cent to 8 per cent affected life business, as the assumed rate of interest of most products in force was over 10 per cent. After this great shock, most life products have been redesigned with sliding scale structure to cope with changes in bank interest rates.

The underwriting results of non-life business for 1985-89 show a decline in the share of earned premium in total income as in the case of life business during the period, though the weight of investment income is not as high as life business. The incurred loss ratio compared to the total income had moderate fluctuations with an average of 66.7 per cent, while the net expense ratio has been keeping the relatively low level of 25-27 per cent. Net profits have been realized only in the last three years, since there had been a major defecit in motor business in the two preceding years.

F. Assets and investment

The total invested assets of life business have been growing at an average rate of 33.1 per cent during the period and reached 21.8 trillion won (equivalent to $31 billion) at the end of the underwriting year 1989. The size of invested assets compared to premium income has slightly increased from 1.7 times in 1985 to 1.8 times in 1989, which is still lower than the average level in most dveloped countries (three times), as the average term of life policies are relatively short (5-10 years). The largest part of the assets of life companies is invested in loans and securities though the weight of securities has been increasing as the yield in stock has become higher than loans in later years. The profit ratio shows a constant increase until 1988 due to high yields in stock investment.

Total assets in non-life business have grown during the period at an average rate of 34.4 per cent, reaching 3,028 billion won (equivalent to $4.3 billion) at the end of 1989. The size of assets compared to premium income increased from 79 per cent to 115 per cent during the period. However, the level of assets is still lower than the average level

in most developed countries, estimated to be over 1.5 times. In contrast to life business, the majority of non-life assets are invested in securities and deposits, though the weight of loans has been moderately increasing, since non-life business requires more liquidity than life business. The profit ratio of investment has shown the same pattern as life business.

G. Trade in reinsurance

Trade for both domestic and international reinsurance in Korea has been controlled by the Government since the establishment of Korean Reinsurance Corporation (KRIC), the sole reinsurance specialist in Korea, in 1963. The objective of this regulation was to strengthen the domestic capacity and to reduce the outflow of foreign currency to developed markets.

This regulation has been gradually relaxed, particularly since 1978, when KRIC was totally privatized from being a semi-government structure. Compulsory cession to KRIC was phased down from 30 per cent in 1987 to 20 per cent in 1989, in the case of fire, marine and engineering insurance, and total liberalization was realized in April 1990.

In non-life business, the outward reinsurance premium compared with domestic written premium has considerably declined from 15.7 per cent in 1984 to 6.9 per cent in 1988 as the capacity for local retention grew with the size of the market. The volume of inward reinsurance premium has declined from 5.5 per cent in 1984 to 0.9 per cent in 1988, mainly due to excessive deficits in most reinsurance markets abroad. Accordingly, the net domestic-retention ratio increased from 89.8 per cent in 1984 to 94.0 per cent in 1988. This implies a noteworthy decrease in dependancy on developed markets.

In overseas reinsurance, the Korean market lost $114 million in inward (or export), and $236 million in outward (or import) in reinsurance from 1985 to 1989, making a total of $350 million deficit in net balance. This figure represents -30.6 per cent of the total amount of trade.

Table 4 shows ten major importing countries of reinsurance in 1988. United Kingdom is leading outward reinsurance with a share of

58.6 per cent, followed by the United States and Japan. The aggregate share of these three devloped markets reached 74.7 per cent.

Table 5 shows ten major exporting countries in 1988. The largest exporting country was Japan, with a share of 27.0 per cent, followed by nine other countries making an aggreagte share of 75.8 per cent. This means that the market is much more diversified in export than in import. However, most markets showed deficit in net balance, with a few exceptions such as Hong Kong, the Federal Republic of Germany and India.

H. Competitiveness and concentration

Table 6 shows the change in market shares of life companies in the last five years. The market had been shared among six domestic companies for over 20 years as the government did not allow any new entry during the period. Samsung, the largest company, maintained the share of over one-third and the "top three" dominated the market with a share of over three quarters. After the liberalization of 1987, 19 companies newly joined the market, making a total of 25 companies as of March 1990. They can be grouped into five categories:

- Six companies that existed before the opening of market in 1987;
- Six national companies, newly licensed in 1989 with headoffices in Seoul covering nation-wide;
- Four local national companies, licensed in 1988 with headoffices in local cities;
- Five joint-venture companies, newly licensed in 1989; and
- Two branch offices and two subsidiaries of United States companies, licensed after liberalization (1989-90).

It is too early to make judgements on competitiveness, as most newly licensed companies have been in operation only for a few years or even a few months. But the trend so far shows that the first group listed above is still dominating the market with an aggregate share of over 94 per cent even after the market has been opened.

The concentration of business is unique in life business. Here, the largest company - Samsung Life - has been maintaining a share of over 33 per cent for nearly 25 years. The aggregate share of the "top three" has been over 70 per cent, though their shares have declined slightly since liberalization. "Korea Life", however, is an exception to this. Such a distinct concentration can be attributed to three major reasons: (a) buyers' preference for reputable companies as more reliable, (b) experienced and aggressive sales forces, and (c) efficient management as the result of economies of scale.

Table 7 shows the market shares change of 15 non-life companies in the last five years. The largest company "Korea Auto" has been leading the market though its share has been declining since 1983, when the monopoly of motor business was ended and 10 other general companies and 2 foreign branches were allowed to write multiple lines except surety business. Nonetheless, the top four companies still maintain an aggregate share of over 50 per cent, and the next eight companies have a moderate share of 3-9 per cent each.

It is worth noting that the share of the two United States branches has never been over 1.5 per cent of the market, though they have been in operation for over ten years. There are three companies in the first group mentioned above, in which three foreign companies (from the United States, Japan, and the United Kingdom) have equity participation between 12.9 per cent to 18.1 per cent of the issued shares. If those equities can be considered as part of the foreign share of the market, the total foreign share in the non-life market can be estimated to be 4 per cent, together with the share of two freign branch offices.

Another aspect of competitiveness in non-life business can be seen in marine cargo insurance, as this coverage can be obtained both domestically and internationally, depending on the terms of trade in goods. Though the government encourages to purchase domestic coverage, most trading companies decide in favour of better rate and service in choosing their insurers. The volume of international trade in goods increased more than twice in the recent five years, from $51 billion in 1983 to $113 billion in 1988. The ratio of the amount insured domestically to the total amount of trade has slightly declined from 61.1 per cent to 57.8 per cent during the period, while the cargo insurance premium increased more than twice to reach $183 million in 1988. These

figures imply that local companies have maintained their relative advantage in competitiveness with other developed markets.

I. Participation in international market

Table 8 shows the participation of Korean insurance firms in the international market as of 31 March 1990. Though there are 30 offices in seven countries, only nine entities are engaged in either direct or reinsurance business in these countries. The volume of premium in direct business in 1989 was compiled as won 6.9 billion (equivalent to $10 million), which is only 0.3 per cent of domestic non-life business, or even less than 10 per cent of the above-mentioned share of foreign firms in the domestic market.

II. ANALYSIS ON REGULATORY AND NON-REGULATORY BARRIERS TO THE EXPORT OF SERVICES

A. Regulatory barriers

Korean insurance market had a relatively uncontrolled structure until 1962, with 10 life and 14 non-life companies with the nominal average capital of 11 million won (equivalent to $85,000) competing in a market of $13 million. The market was totally restructured in 1962, after a special inspection by the government for strengthening the financial structure in order to support the first five-year economic development plan launched in that year. This policy included:

- Reduction in the number of companies by encouraging merger and acquisition;
- Increase of minimum capital to 100 million won;
- Enforcement of compulsory motor-liability insurance;
- Localization of all insurance purchases;

- Establishment of a State-owned reinsurance corporation (KRIC); and

- Enforcement of compulsory reinsurance, both domestic and overseas.

After this reformation, one reinsurance, six life, and 12 non-life companies were maintained. In 1977, the first two foreign companies - AIG and CIGNA (United States) - were allowed to establish their branch offices to underwrite limited lines (non-marine alone in the first five years). Three national companies were also allowed to conclude joint-venture agreements with three foreign companies: Royal (United Kingdom) in 1977, Tokio (Japan) in 1979, and Continental (United States) in 1980. While these five foreign companies were allowed to participate in domestic non-life business, local companies were also allowed to establish their offices in Japan (1976), London (1978), Singapore (1978), and other places in the form of branches, subsidiaries or joint-ventures.

Liberalization of life business, on the other hand, was delayed until 1987 after the exertion political pressure by the United States Government and the subsequent negotiations between the Korean Government and the United States Trade Representative. The Ministry of Finance published the following guidelines in 1987 and 1988.

- Guideline for Licensing a Foreign Insurance Company's Branch Office in Korea (15 June 1987);

- Guideline for Licensing a Joint-Venture Life Insurance Company in Korea (18 March 1988); and

- Guideline for Licensing a Foreign Non-life Insurance Company's Branch Office in Korea (17 June 1987).

These guidelines specify requirements concerning (a) qualifications, (b) documentation required for application, (c) considerations for the preparation of application documents, (d) examination of documentation, (e) operating funds or capital required, (f) request for increase in operating fund and its permission, (g) period and renewal of license, (h) representative and actuary in Korea, (i) duty to compensate a deficit

carried forward, (j) remittance of profits, (k) management of assets, and (l) solvency-margin control system. Based on these guidelines, six foreign life companies (four branches and two subsidiaries) and six joint-venture life companies have obtained licenses during the period 1987-90, as shown in table 1.

What I have given above is a brief review of the progressive liberalization in market access or establishment in the past. At present there are 48 insurance companies, all of them private - 34 national, 6 joint-venture and 8 foreign - licensed to do business under a non-discriminatory legal framework.

In "across-the-border" trade, reinsurance transaction - both domestic and international - has been totally liberalized from 1 April 1990, and transport insurance (or marine cargo) integral to goods trade has been opened for free competition as mentioned earlier. In sum, as far as explicit laws, regulations and guidelines are concerned, regulatory barriers are no longer prevalent in the Republic of Korea.

B. Non-regulatiory barriers

There are several political and economic barriers for foreign entities, arising from the implementation of laws and regulations on the establishment and conduct of business in the Republic of Korea.

The first among such barriers is the difficulty in obtaining licenses. The licensing of the 13 United States companies was largely a result of political pressure, generated in the context of the United States' deficit in goods trade. However, other countries except Canada, United Kingdom and Japan have not yet established their offices in Korea. For new foreign companies who wish to enter the market, this is likely to remain an obstacle. However, many observers feel that the increase in suppliers has already exceeded the growth in demand.

It has been argued that foreign entities experience unfair treatment in the conduct of business - e.g. in the introduction of new products, investment in real estate, increase of capital, enforcement of dividend, lack of government support in labour disputes, etc. However, it is difficult to identify these barriers objectively, since similar issues are often raised by national firms as well.

C. Restrictive business practices

Market-sharing arrangements in fire insurance pool for high-rise buildings and certain industrial complexes seem to restrain free competition in this area. The solution that was initially agreed involved the inclusion of two foreign branches with equal share, but national companies later decided on a phased dissolution for open competition which is still in process.

The recruitment of experienced manpower has been another issue since the emergence of many new firms in recent years. After multilateral negotiations, companies finally agreed not to scout more than 25 per cent of total employees from competitors.

Foreign life companies are not as yet accepted as full members of the Life Insurance Association, but are accepted as associate members without vote. This means that there is a certain discrimination with respect to the right to self-regulation between national and foreign companies.

III. INCREASING COMPETITIVENESS AND EXPANDING THE INTERNATIONAL MARKET

A. Stages of insurance development

As Rodney Grey rightly points out, in contrast with "traded goods" which can be considered as one category, "traded services" comprise a series of dissimilar categories.[2] They are mostly related to man, money, information and transportation. Insurance is a service primarily related to money. But the demand for insurance is determined by all the other factors closely related to various stages of economic development in different countries.[3]

2 Rodney de C. Grey, *The Services Agenda* (Halifax: Institute for Research on Public Policy, 1989), p. 45.

3 Un Hoe Park, "A Survey on the Income Elasticity of Insurance Demand", *Korea Non-life Insurance*, No. 16 (February 1989), pp. 22-35.

Insurance can be classified into three broad categories in relation to the concept of trade.

- *Related to traded goods,* such as goods in transit (or cargo insurance), product liability, and export credit insurance.

- *Across-the-border trade,* such as international reinsurance and purchase of primary insurance from another country.

- *Pure domestic trade* in all kinds of insurance and reinsurance other than the two groups mentioned above.

In other words, insurance can be partly integral to goods trade (probably less than 2 per cent in volume), and can also be an international trade in itself (probably less than 5 per cent). But the major portion (more than 90 per cent) is a pure domestic trade which has no direct relation to the international economy.

An insurance product does not require intellectual property right in design, even though most developing countries need internationally accepted policy forms or tested new products. Developing countries certainly need technical assistance from developed countries in product design, in rating industrial risks, and in reinsurance capacity, but do not really need the services of developed countries in retailing life or motor insurance. Therefore, to be beneficial for all parties, negotiations should be based on the consideration that the liberalization of insurance market needs to be phased according to the stages of insurance development in different countries, and not on a uniform or reciprocal basis.

Table 9 shows the correlation between premium and GNP for selected countries in 1987. They are classified into four groups based on per capita GNP:

- Group A: *Highly developed stage,* with per capita GNP of over \$10,000.

- Group B: *Developed stage,* with per capita GNP between \$5,000-10,000.

- Group C: *Developing stage,* with per capita GNP between \$2,000-5,000.

- Group D: *Least developed stage,* with per capita GNP of less than $2,000.

The ratio between premium and GDP is often used for measuring the stage of development. However, many specific cases have shown that this criterion is not always valid. For example, Ireland marked the highest Premium/GDP ratio of 12.24 per cent in 1987. But this does not mean that Ireland is the most developed nation in the world. The Republic of Korea also showed a higher ratio than Japan and the Federal Republic of Germany, but the per capita premium was only 1/7 of Japan and 1/5 of the Federal Republic of Germany.

Therefore, the criterion for determining the stage of insurance development should be the level of per capita premium rather than the Premium/GDP ratio. A possible grouping is suggested below:

- Group A: *Developed stage,* with per capita premium of over $600.

- Group B: *Developing stage,* with per capita premium of between $100-600.

- Group C: *Underdeveloped stage,* with per capita premium of less than $100.

According to the estimations of Swiss Reinsurance Company for the year 1987,[4] Group A encompasses 18 developed countries most OECD members, and Group B includes 12 developing countries and territories, such as the Republic of Korea, Singapore, and Taiwan, Province of China. All the remaining countries are grouped in category C.

According to this criterion, Korea belonged to Group C until 1983, joined Group B in 1984, and will probably be included in Group A in early 1990s. See table 10.

B. Phased liberalization

Liberalization of trade in insurance can proceed in three phases, in accrodance with the stages of development discussed above. "Phase

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4 Swiss Reinsurance Company, *Sigma*, May 1989.

I" can be applied to Group C (underdeveloped stage) countries. Countries in Group C still need technical assistance and reinsurance support from those in Groups A and B, in strengthening their infant market in order to meet the needs of their domestic economies. Technical assistance could include education, product design, pricing, marketing and reinsurance. Here, liberalization can be limited to free purchase of "goods in transit insurance" (related to trade in goods), international reinsurance for the surplus of their domestic retention, and establishment of foreign brokers and liaison offices.

"Phase II" can be applied to Group B (developing stage) countries. Countries in this Group can probably afford a limited degree of competition with other countries in Groups A and B, in order to provide local consumers with multiple options in product, price and service. Liberalization in this phase can include free international reinsurance and a limited establishment of foreign insurance companies, preferably in the form of joint ventures with local residents.

"Phase III" will be the final stage to be applied only to Group A (developed stage) countries. This phase will eventually aim at a "totally free and competitive market", with the proposed principles of transparency, non-discrimination and national treatment.

C. Role of the governments

The objectives of governments can be somewhat different in different countries, depending on their respective stage of insurance development. Group C countries require protection of local industry and domestic economy. Group B countries can encourage their industry to enhance competitiveness so as to meet the changing needs of consumers. Most Group A countries are under pressure from both the industry and the consumers to deregulate and ensure free competition not only among insurers, but also with other financial institutions.

The role of the government, particularly in developing countries, is vital in the sound development of insurance industry, as several important activities such as product design, price, distribution, reinsurance and investment are all under the strict supervision of government in most countries.

One major aspect of the governmental role will be the control in number of insurance companies. Table 11 shows the average size of insurance companies in selected countries in terms of premium. The average of G5 countries in 1987 was $106.8 million, which is higher than the world average of $79.4 million, while the ASEAN avearage was $8.4 million or 1/9 of the world average. This implies that the economies of size must be considered in determining the number, particularly when the policy goal is to increase competitiveness.

A second consideration concerns capital requirement and retention control, particularly in the field of non-life insurance, as the fluctuation of loss ratio in this sector is generally greater than in life business. The minimum capital can be determined with Kenny's rule of 3 to 1. In other words, the total domestic premium can be divided by 3 to determine the total capital requirement, and this figure can be further divided by the number of companies to determine the minimum capital of each company.

The maximum number of foreign companies to be licensed is another important consideration. Table 12 shows the market structure of selected countries in terms of the number of domestic and foreign companies. The world average ratio of foreign companies was 17.3 per cent in 1985. It is worth noting that the G5 countries had only 12.9 per cent foreign companies in their territory, but established branches abroad more than 1.5 times in number. Five ASEAN countries, on the other hand, had 75 foreign companies or 18.3 per cent of total number, but their number of branches abroad was only 26 or 1/3 of foreign companies in their territory. Likewise, the Republic of Korea now has 14 foreign companies licensed to do business, but established only 8 branches aborad. The maximum number of foreign companies can ideally be determined in relation to the establishment of domestic companies abroad on a reciprocal basis. An alternative rule could be that the maximum number of foreign companies cannot exceed 1/2 of domestic companies or 1/3 of the total number, which is nearly twice the world average (17.3 per cent).

Once the economies of scale are achieved in relation to the aforesaid criteria, the next step will be how the competitiveness of suppliers can be maintained and enhanced in order to cope with pressures from both domestic consumers and foreign competitors.

Competitveness in any business can be obtained from four basic factors: (a) quality product, (b) economically feasible price, (c) effective marketing, and (d) up-to-date technology.

Thus the role of governments in increasing the competitiveness of their local industry will also be four-fold. To improve the quality of products, the government should encourage local insurers to invest in research and development activities, including the employment of experts (domestic and foreign), market research on developed economies, and creative design to meet the needs of local culture and mentality.

Comparative advantage in price can be obtained by accurate assessment of risks, efficient investment, and expense control through economies of size. Korean life companies achieved the average investment profit ratio of 13.6 per cent and maintained an expence ratio below 12 per cent in 1985-89. These two factors enabled six existing companies to show profit and yet maintain a market share of over 94 per cent even after liberalization.

Once product and prices are set, marketing will determine the share. Korean life companies achieved an impressive average growth rate of 35.9 per cent in 1984-89, most probably due to their aggressive sales force of over 200,000 people, 90 per cent of whom are housewives. They are paid both fixed salary plus commission on their production, and producing nearly 90 per cent of new business. This is in contrast with the case of non-life market, where 55 per cent of the business is produced by agents. This implies that the most efficient distribution channel can vary, depending on the line of business and on the social background of the respective country. Therefore, diversification can be attempted to determine the optimum mix.

The final aspect of competitiveness is related to technology including (a) risk managment consulting, (b) selection of risk, (c) determination of retention, (d) reinsurance, (e) information management, and (f) claims settlement. These areas require continued systematic research and education on a long-term basis.

D. Implications for the Uruguay Round negotiations

Three questions can be raised in relation to the text of the Punta del Este Ministerial Declaration of September 1986 and to the United States proposal of October 1987, regarding the insurance sector:

- Will progressive liberalization be of benefit to every country, regardless of its stage of economic development? (General Consideration);

- Can time-phased liberalization be applied to all signatories at the same time? (Non-discrimination); and

- Does national treatment mean the possible inflow of limitless number of foreign service providers even to dominate the local market? (National Treatment).

The United States proposal suggested that the framework should be of benefit to every country, regardless of its stage of economic development. According to *Sigma* statistics, the share of G7 countries was over 82 per cent of the world premium in 1987, which means that all other countries share the remaining 18 per cent - less than half of United States share (38.00 per cent).

If the proposed liberalization is implemented in the insurance sector, the share of G7 will certainly increase due to their comparative advantage in free competition, and the difference between G7 and all other countries will be greater even though their active participation may promote the growth of other countries through the provision of better products and services. It will also affect the balance of payments and domestic capital formation in developing countries, conflicting with their policy objectives for balanced development. Therefore, it can be concluded that progressive liberalization in the insurance sector can only be of benefit to a limited number of countries which have already reached a certain stage of insurance development.

The second question is that of non-discrimination. Developed countries have taken the position that signatories to the framework agreement should extend the benefits of the agreement unconditionally

to all signatories. This means that once the agreement is signed, all countries must open their market at the same time according to a timetable, even if limited exceptions may be considered. As already discussed, most developing countries still need technical assistance and reinsurance support from developed countries. Therefore, a realistic approach will be the phased liberalization depending on the stages of insurance development. If the criteria to determine such stages can be agreed, as proposed earlier, the result will not be discriminatory, as the same rule could apply to several relevant signatories.

The third question concerns national treatment. The final stage of liberalization may include free cross-border movement and free establishment. This stage may bring chaos in most developing countries as developed-country firms may compete with one another to dominate the local markets. Therefore, national treatment must be limited to certain lines of business such as large industrial risks in case of cross-border trade, and be limited to a certain number of companies in case of establishment, as proposed earlier.

The Republic of Korea is a developing country in the sense that per capita income is still at the level of $5,000. However, its world rank in terms of insurance premium was already 11th in 1987. This does not mean that Korea reached the developed stage, as its per capita premium was only 1/6 of United States level (see table 9). Korea allowed the establishment of 12 foreign life compamies since 1987, and also liberalized reinsurance trade since April 1990. This means that the Republic of Korea is already on the phase of progressive liberalization. However, the proposed non-discrimination may require the further opening of market to all other developed countries. Such a sudden landslide will clearly result in over-supply and perilous competition.

These considerations clearly suggest that the Uruguay Round negotiations need to be based on the notion of a positive list, which would permit a phased liberalization, depending on the respective stage of insurance development of different contracting parties.

Table 1

NUMBER OF INSURANCE COMPANIES IN KOREA

Classification	Types of Business	Numbers in 1986	New entries 1987	1988	1989	1990	Sub-Total	Number in 1990
National companies	Life	6	-	4	10	-	14	20
	Non-Life	13	-	-	1	-	1	14
	Total	19	-	4	11	-	15	34
Joint Ventures	Life	-	-	-	5	1	6	6
	Non-Life	-	-	-	-	-	-	-
	Total	-	-	-	5	1	6	6
Foreign companies	Life	-	2	-	3	1	6	6
	Non-Life	2	-	-	-	-	-	2
	Total	2	2	-	3	1	6	8
Total	Life	6	2	4	18	2	26	32
	Non-Life	15	-	-	1	-	1	16
	Total	21	2	4	19	2	27	48

Source: Insurance Bureau, Ministry of Finance, *Major Insurance Statistics*, April 1990.

Table 2

EMPLOYMENT IN INSURANCE SECTOR

	March 1989			March 1990			Increase (Per cent)		
	Life	*Non-Life*	*Total*	*Life*	*Non-Life*	*Total*	*Life*	*Non-Life*	*Total*
Number of companies	8	15	23	25	16	41	212.5	6.7	78.3
Number of Branches	6,502	1,834	8,336	7,657	2,209	9,866	17.8	20.4	18.4
Number of Company Staff	27,037	16,126	43,163	31,999	18,659	50,658	18.4	15.7	17.4
Number of Solicitors	175,594	23,246	198,840	210,284	34,010	244,294	19.8	46.4	22.9
Number of Agents	357	16,106	16,463	1,122	21,025	22,147	214.3	30.5	34.5
Total Employment [a]	203,702	87,690	291,392	245,649	115,744	361,393	20.6	32.0	24.0

Source: Insurance Supervisory Board, *Monthly Insurance Review*, May 1989 and May 1990.

[a] It is assumed that on average one agent employs 3 persons.

Table 3

CORRELATION BETWEEN GDP AND PREMIUM

Year	GDP (billion dollars)	Per Capita GNP (dollars)	Life Premium/ GDP (per cent)	Non-life Premium/ GDP (per cent)	Total Premium/ GDP (per cent)
1984	85.5	2,044	4.48	1.27	5.75
1985	86.8	2,047	5.28	1.35	6.63
1986	98.3	2,300	6.41	1.38	7.79
1987	131.8	3,110	6.73	1.42	8.14
1988	175.2	4,127	7.33	1.50	8.83
1989	202.6	4,968	8.34	1.85	10.19

Source: Bank of Korea, *Major Economic Indicators*; Insurance Supervisory Board, *Monthly Insurance Review*.

Table 4

MAJOR IMPORTING COUNTRIES OF REINSURANCE (1988)
(Premium in thousand dollars)

Bank	*Country*	*Premium (A)*	*Share (per cent)*	*Net Balance (B)*	*B/A (per cent)*	*Aggregate Share (per cent)*
1	United Kingdom	116,327	58.6	-30,425	-26.2	58.6
2	United States	19,956	10.1	-8,704	-43.6	68.7
3	Japan	11,851	6.0	-1,933	-16.3	74.7
4	Hong Kong	9,630	4.9	-1,966	-20.4	79.6
5	Fed. Rep. of Germany	9,530	4.8	-2,593	-27.2	84.4
6	Burmuda	8,654	4.4	-4,184	-48.3	88.8
7	Switzerland	8,645	4.4	-3,438	-39.8	93.2
8	France	2,821	1.4	-1,050	-37.2	94.6
9	Italy	1,804	0.9	-924	-51.2	95.5
10	India	1,460	0.7	-267	-18.3	96.2
	Other	7,691	3.9	-15,093	-196.2	100.0
	Total	198,369	100.0	-70,577	-35.6	-

Source: Korean Reinsurance Company.

Table 5

MAJOR EXPORTING COUNTRIES OF REINSURANCE (1988)
(Primium in thousand dollars)

Bank	Country	Premium (A)	Share (per cent)	Net Balance (B)	B/A (per cent)	Aggregate Share (per cent)
1	Japan	7,432	27.0	-178	-2.4	27.0
2	United Kingdom	2,948	10.7	-7,992	-271.1	37.7
3	Hong Kong	1,853	6.7	362	19.5	44.4
4	United States	1,818	6.6	-6,319	-347.6	51.0
5	Fed. Rep. of Germany	1,711	6.2	339	19.8	57.2
6	Switzerland	1,656	6.0	-189	-11.4	63.2
7	Singapore	920	3.3	-410	-44.6	66.5
8	Italy	908	3.3	-53	-5.8	69.8
9	India	901	3.3	267	29.6	73.1
10	Thailand	734	2.7	-38	-5.2	75.8
	Other	6,677	24.2	606	9.1	100.0
	Total	27,558	100.0	-13,605	-49.4	-

Source: Korean Reinsurance Company.

Table 6

MARKET SHARES OF NON-LIFE COMPANIES
(Shares in percentage)

Group	Companies	Year of Entry	1984 Share	1984 Aggregate	1989 Share	1989 Aggregate	Foreign Equity (per cent)
A	Samsung	1957	36.5	36.5	33.4	33.4	-
	Daehan Kyoyuk	1958	26.8	63.3	20.5	53.9	-
	Rep. of Korea	1946	13.4	76.7	18.0	71.9	-
	Jeil	1954	8.2	84.9	7.9	79.8	-
	Hungkuk	1958	8.1	93.0	7.8	87.6	-
	Dong-Ah	1973	7.0	100.0	6.5	94.2	-
Sub-Total		-	100.0	100.0	94.2	94.2	-
B	6 New domestic companies	1989	-	-	2.2	96.4	-
C	4 New local companies	1988	-	-	1.9	98.3	-
D	5 Joint venture companies	1989	-	-	1.6	99.9	49-60
E	4 Foreign branches and subsidiaries	1987-90	-	-	0.1	100.0	100
Total (25 companies)		-	100.0	100.0	100.0	100.0	-

Source: Insurance Supervisory Board, *Monthly Insurance Review*, various issues.

Table 7

MARKET SHARES OF NON-LIFE COMPANIES
(Shares in percentage)

Group	Companies	Year of Entry	1984 Share	1984 Aggregate	1989 Share	1989 Aggregate	Foreign Equity (per cent)
A	Korea Auto	1968	26.4	26.4	15.0	15.0	-
	Akuk Fire	1952	9.6	36.0	13.2	28.2	-
	Hyundai Marine	1955	8.9	44.9	12.5	40.7	-
	Lucky Fire	1959	8.8	53.7	11.3	52.0	-
	Oriental Fire	1922	8.2	61.9	8.7	60.7	18.1
	Daehan Fire	1946	5.3	67.2	6.1	66.8	-
	First Fire	1949	5.6	72.8	5.7	72.5	14.3
	Shindong-A	1946	4.7	77.5	5.6	78.1	-
	International	1947	6.3	83.8	5.1	83.2	-
	Koryo Fire	1948	6.3	90.1	4.9	88.1	12.9
	Haedong Fire	1953	3.5	93.6	3.4	91.6	-
B	Korea Fidelity	1969	5.1	98.7	7.3	98.9	-
	Hankuk Fidelity	1989	-	-	0.1	99.0	-
C	American Home	1968	0.8	99.5	0.7	99.7	100
	CIGNA	1968	0.3	99.8	0.3	100.0	100
Total (15 companies)		-	100.0	100.0	100.0	100.0	-

Source: Insurance Supervisory Board, *Monthly Insurance Review*, various issues.

Table 8

KOREAN FIRMS IN INTERNATIONAL MARKETS
(As of 31 March 1990)

Types	*Countries*	*No. of Entry*	*Year of Entry*
Branch Office	United States	3	1968-90
	Japan	1	1976
	Singapore	1	1978
Subsidiary	United Kingdom	1	1978
Joint Venture	Malaysia	1	1977
	Thailand	1	1980
	United States	1	1980
Liaison Office	United States	7	1979-90
	United Kingdom	7	1972-90
	Japan	6	1976-90
	Hong Kong	1	1989
Total	7	30	1968-90

Source: Ministry of Finance, Insurance Bureau, *Major Statistics and Information*, April 1990, p. 87.

Table 9

CORRELATION BETWEEN PREMIUM AND GNP/GDP IN SELECTED COUNTRIES IN 1987
(In dollars)

Group	*Country*	*GNP/ Capita [a] (A)*	*Premium/ Capita [b] (B)*	*B/A (per cent)*	*Premium/ GDP [b]*
	United States	18,413	1,668.2	9.06	9.07
	Japan	19,530	1,974.5	10.11	8.69
	Fed. Rep. of Germany	18,402	1,329.9	7.23	6.40
A	United Kingdom	11,927	1,121.8	9.41	8.35
	France	15,785	898.8	5.69	5.06
	(Average)	(16,811)	(1,398.6)	(8.30)	(7.51)
	Spain	5,869[c]	279.6	4.76	3.31
	Singapore	7,872	223.3	2.84	2.78
	USSR	8,410[c]	102.7	1.22	2.80
B	Ireland	5,080[c]	1,145.5	22.55	12.24
	Israel	6,210[c]	444.6	7.16	5.40
	(Average)	(6,688)	(439.1)	(7.71)	(5.31)
	Rep. of Korea	3,100	264.8	8.51	8.85
	Taiwan, Prov. of China	4,962	164.8	3.32	3.33
	Argentina	2,350[c]	26.4	1.12	1.80
C	Venezuela	2,930[c]	61.2	2.09	2.26
	Portugal	2,230[c]	101.7	4.56	2.69
	(Average)	(6,688)	(439.1)	(7.71)	(5.31)
	(Average)	(3,116)	(123.8)	(3.92)	(3.79)
	Malaysia	1,600[c]	58.2	3.64	2.98
	Thailand	847	12.2	1.44	1.35
	Brazil	1,950[c]	10.8	0.55	0.86
D	Mexico	1,598[c]	11.1	0.69	1.02
	Egypt	1,240	13.0	1.05	1.05
	(Average)	(1,447)	(21.1)	(1.47)	(1.45)

Source:
a IMF, *International Financial Statistics*, various editions.
b Swiss Reinsurance Company, *Sigma*, May 1989.
c 1986.

Table 10

DEVELOPMENT STAGES OF KOREAN MARKET

Year	GNP/Capita (A)	Premium/Capita (B) dollars	B/A (per cent)	Premium/GNP (per cent)	Stage
1970	252	2.8	1.12	1.04	C
1971	288	2.3	0.81	0.84	C
1972	318	3.7	1.15	1.18	C
1973	395	5.7	1.45	1.45	C
1974	540	6.4	1.18	1.41	C
1975	590	8.3	1.40	1.40	C
1976	797	11	1.34	1.34	C
1977	1,008	15	1.52	1.52	C
1978	1,392	25	1.79	1.87	C
1979	1,640	43	2.61	2.53	C
1980	1,589	39	2.48	2.70	C
1981	1,719	52	3.04	3.14	C
1982	1,773	79	4.44	4.57	C
1983	1,914	97	5.07	5.23	C
1984	2,044	118	5.78	5.96	C
1985	2,047	138	6.73	6.87	B
1986	2,300	192	8.34	8.04	B
1987	3,110	281	9.04	8.33	B
1988	4,127	401	9.71	8.95	B
1989	4,968	487	9.80	10.28	B

Source: Bank of Korea, *Statistical Yearbook*, various editions; ISB, *Monthly Insurance Review*, various editions.

Table 11

AVERAGE SIZE OF INSURANCE COMPANIES IN SELECTED COUNTRIES

Country	*Premium in 1987* [a] *(million dollars)*	*Total number* [b] *of Companies (1985)*	*Average Size (million dollars)*
United States	406,652	6,093	66.7
Japan	241,069	86	2,803.1
Fed. Rep. of Germany	81,353	516	157.7
United Kingdom	63,820	712	89.6
France	50,000	482	103.7
G5 Total	842,894	7,889	106.8
Malaysia	963	62	15.5
Singapore	583	64	9.1
Thailand	653	74	8.8
Indonesia	642	80	8.0
Philippines	605	128	4.7
ASEAN Total	3,446	408	8.4
World Total	1,070,100	13,484	79.4
Rep. of Korea [c]	20,659	48	430.0

a Premium: *Sigma*, May 1989.
b No. of Companies: *Sigma*, November/December 1985.
c Premium: 1989, No. of Companies: as of June 1990.

Table 12

MARKET STRUCTURE OF SELECTED COUNTRIES

Country	Domestic Companies A	Foreign Companies B	Total No. of Companies C	Branches Abroad D	B/C (per cent)	D/B (per cent)
United States	5,791	302	6,093	579	5.0	191.7
Japan	44	42	86	64	48.8	152.4
Fed. Rep. of Germany	404	112	516	122	21.7	108.9
United Kingdom	634	78	712	608	11.0	779.5
France	318	164	482	166	34.0	101.2
G5 Total	7,181	1,016	7,889	1,539	12.9	151.5
Malaysia	49	13	62	5	21.0	38.5
Singapore	23	41	64	13	64.1	31.7
Thailand	69	5	74	1	6.8	20.0
Indonesia	80	-	80	1	-	-
Philippines	112	16	128	6	12.5	37.5
ASEAN Total	333	75	408	26	18.4	34.7
World Total	11,152	2,332	13,484	2,332	17.3	100.0
Rep. of Korea [a]	34	14	48	8	29.2	57.1

Source: *Sigma*, November/December 1985.
a As of June 1990.

TRADE IN BANKING SERVICES: ASEAN COUNTRIES

*Mario Lamberte**

INTRODUCTION

Since its establishment in 1967, ASEAN has enjoyed regional peace and stability. This has been translated into high economic growth envied by other regional groupings. ASEAN is however composed of countries at different levels of development and degrees of sophistication of economy. Singapore has a per-capita GNP in 1988 more than 20 times higher than that of Indonesia, the lowest in the region. It was also the fastest growing ASEAN member country in the 1980s. Thailand's phenomenal economic growth in the 1980s is likely to be sustained in the early 1990s when the huge foreign investments it received in the late 1980s are translated into increased productive capacity. In the Philippines, the political and economic turbulence has hampered its development and a large outstanding debt will continue to constrain its growth in the medium term.

Financial deepening has taken place in ASEAN countries in 1980s. Indonesia, Malaysia and Thailand experienced a doubling of the ratio of broad money to GNP, which is used here as a rough measure of financial deepening. Singapore has continued its process of financial deepening. Again, the only exception in this impressive performance of ASEAN countries is the Philippines. A liquidity crisis struck the Philippine economy in 1981, followed by a severe balance-of-payments problem in the mid-1980s. These resulted in the collapse of several financial institutions, which shook the people's confidence in the banking system and led to capital flight.

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Over the past three decades, ASEAN economies have undergone a process of structural transformation, shifting their dependence from agriculture to non-agricultural activities. The service sector has increasingly become an important productive sector in their economies. In 1989, the share of the service sector in the GDP of ASEAN countries ranged from 39 to 63 per cent. Their contribution to employment in ASEAN countries has also been significant. Quibria underscores the importance of the service sector in economic development:

> The role of services in economic development is far from unilinear. In many cases, the development of services is not a consequence but a cause of growth. For example, an efficient financial sector, an extensive transportation and telecommunication network and well-run public administration: all are preconditions of growth and development. So is a well-developed infrastructure of health and education services. Traditionally, the service sector has not been the subject of conscious comprehensive planning. As a consequence, a lack of planning may result in the initial underdevelopment of key services.[1]

The experience of Singapore serves to demonstrate that the service sector itself can be a growth sector.

However, the quantity and quality of the products produced by the service sector of ASEAN countries vary greatly among one another. In Singapore, technology-intensive services (e.g. banking and telematics) are quite significant, while in Indonesia, the Philippines and Thailand, there is a predominance of traditional, labour-intensive services (e.g. restaurants, retailing, etc.). Such diversity reflects the varying levels of economic development among ASEAN countries.

Trade in services has now become a subject of the new round of multilateral negotiations. The issue here is basically similar to the one that emerged in earlier rounds of negotiations on trade in goods, i.e. gradually dismantling barriers to trade in services in such a way that both developed and developing economies can benefit. This undertaking is far from easy. Firstly, trade in services is overwhelmingly dominated by developed economies, and developing countries may feel apprehensive about further liberalization in this sector. Secondly, the service sector is heterogenous and includes areas that are considered

1 M.G. Quibria, "Service Trade and Asian Developing Economies", *Asian Development Bank Economics and Development Resource Center Report Series*, No. 44 (Manila, ADB, October 1989).

politically sensitive. Notwithstanding these, there is a need to examine the issues on trade in services closely so that more enlightened multilateral negotiations can proceed.

This paper focuses on the financial sector. Interestingly, the pattern of net financial flows to ASEAN countries has significantly changed over the last 13 years. Net private flows sharply fell after the explosion of the international debt crisis in 1982. This has some implications on the operations of branches, agencies and representative offices of foreign banks in these countries. It is to be noted that they facilitated the flow of direct foreign investment into these countries and provided banking services to multinational corporations. They were also involved in packaging sovereign loans for ASEAN countries. After the international debt crisis, their activities in these two areas have been considerably reduced because of the slowdown in foreign investment flows and the unattractiveness of sovereign loans.

The banking sector is one of the sectors which is likely to be included in the on-going multilateral negotiations on trade in services. It is envisaged that the pivotal importance which is attributed to the sector and the existence of various different banking services would make the establishment of norms and regulations in the area a particularly complex matter. This paper analyses, in the context of the ASEAN countries, various aspects which are deemed relevant to these negotiations, and explores the possibility of expanding trade in banking services as a means to achieving higher and sustainable economic growth for these countries. More specifically, it examines:

- the scope of banking activities in the ASEAN region;
- the structures of markets and competition;
- the benefits and costs of a more liberal regime for international trade in banking services in the region;
- the implications of the key concepts and principles discussed in the multilateral negotiations on trade in services to the banking sector in the ASEAN countries; and

- the possibility of increasing competitiveness of banks in ASEAN countries and increasing their share of international trade in banking services, including through regional co-operation and the Uruguay Round of trade negotiations on services.

A section will be devoted to each of these specific objectives.

I. SCOPE OF BANKING ACTIVITIES IN THE ASEAN REGION

Although still underdeveloped relative to the financial systems of the OECD countries, the financial systems of ASEAN countries have already achieved a certain degree of sophistication. This may be gathered from the great number and variety of financial institutions that have emerged in ASEAN countries in the last two decades, the multitude of financial services being offered, and the financial instruments that have been created. These developments could be attributed to several factors. One is that ASEAN countries started the process of liberalizing their financial system in the 1970s, albeit at varying degrees and speed. That process is still being pursued at present. The response of the financial systems in ASEAN countries to liberalization have generally been positive. Another important factor is the technological advancement in banking that facilitated the improvement of existing services and resulted in the introduction of new services at a much reduced cost to both banks and customers. The introduction of automated teller machines is one example. Computerization has also allowed banks to offer savings deposit instruments whose interest is compounded daily. Interestingly, this is one area where banking technology developed in advanced economies can be easily copied by less developed countries at least cost, especially if certain infrastructures, such as electricity and telecommunications, are readily available, and if the population are generally well-educated. Yet another factor is the generally impressive economic growth of ASEAN economies which resulted in the changing demand for financial services by the corporate sector, individuals, and institutional investors. This has led to the emergence of new types of financial institutions, - e.g. the merchant banks in Malaysia and Singapore, the offshore banks in the Philippines and Singapore, etc. A wide range of instruments have also been intro-

duced by existing and newly-created financial institutions. Examples of these instruments are bankers acceptances, negotiable certificates of deposits, and other deposit substitutes. Banks have recently expanded their fee-based services or off-balance sheet activities. This is most evident in Singapore, Malaysia, the Philippines and Thailand.

It is to be noted that the monetary authorities and governments in ASEAN countries have played a great role in developing their respective financial infrastructures. In the main, they determine and regulate what kinds of activities a financial institution, whether owned by the government or the private sector, can do. Each type of financial institutions is therefore covered by a specific set of regulations. For prudential reasons, the kinds of activities allowed for different types of financial institutions are associated with different minimum capital requirements. Except for Singapore, governments in ASEAN countries oblige their banks to perform developmental functions. Thus, loan portfolio requirements, that is requiring banks to lend a certain amount of their total loanable funds to specific sectors, are not uncommon in the region.

In general, financial institutions in ASEAN countries may be distinguished by the types of liabilities and assets they are legally allowed to hold. Banking institutions are allowed to mobilize traditional deposits (such as demand, savings and time deposits), whereas non-bank financial institutions are not. Among banking institutions, some are restricted to mobilize only certain types of deposits distinguished by the degree of liquidity, maturity, size, etc. Non-banking institutions are fairly numerous and heterogeneous even within the same ASEAN country. Still, in terms of assets, they are small relative to the banking institutions. However, they have shown to be innovative and have put up competition with banks.

In the past, competition was encouraged, but this was limited only to financial institutions belonging to the same category. This resulted in the segmentation of financial markets. At present, there is a move towards universal banking. This requires the reduction or blurring of distinction among different types of financial institutions. Singapore is way ahead in this new approach, followed by Malaysia and

the Philippines. The on-going financial reforms in Indonesia[2] and Thailand also suggest such a trend.

Table 1 shows banking density ratios in ASEAN countries. It roughly indicates the extent of access of the population of the ASEAN countries to their respective banking systems. The ratio tends to vary inversely with the level of development of the countries concerned; that is, population in more developed ASEAN countries have better access to banking services compared to those in less developed ones.[3] Only Singapore can compare with more developed economies in this area. It is to be noted that most banks and their branches are concentrated in urban areas, leaving the countryside with very little access to banking services. This problem is most acute in Indonesia, the Philippines and Thailand. The numerous and small banks that have been established in the countryside have merely served as conduits of government funds. Hence, they do not truly provide banking services to rural people.

After giving an overview of the banking activities of ASEAN countries, we now briefly describe the scope of banking activities in each of the ASEAN member countries. Less emphasis will be given to activities of non-banking institutions.

A. Indonesia

The financial system in Indonesia consists of deposit money banks, rural financial institutions, savings banks, and different types of non-bank financial institutions.[4] In terms of assets, deposit money banks dominate the financial system.

Deposit money banks may be classified according to ownership. There are five banks that are wholly owned by the Indonesian government. Arndt succinctly describes their activities:

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2 In Indonesia, the deregulation packages were incorporated in PAKTO 27 (October 1988), PAKDES II (December 1988), PAKMAR (March 1989) and PAKJAN (January 1990).

3 In 1982, the density ratio for Australia, New Zealand, United States, and Canada ranged from 3,000 to 6,000 as compared with Singapore's 11,000. But this hides the fact that Singapore also functions as a leading financial center in the region.

4 As of 14 August 1990, the exchange rate was Rp1,845.02 per $1.

> Except in foreign exchange business where the foreign banks are important, the state commercial banks, favoured by a wide variety of privileges, from tax exemptions, subsidies and rediscount facilities to a virtual monopoly of government and other public sector banking business, provide the bulk of banking facilities in their branches all over the country. They hold the major part of demand and time deposits, manage customers' accounts, organize transfers of funds domestically and internationally, cooperate in clearing of inter-bank debts, and conduct the whole range of loan business, from short-term trade credit and personal loans to medium and longer-term loans to the state and private corporate sector.[5]

In addition to what Arndt has mentioned, state commercial banks are also allowed to issue three types of certificates of deposits: discount, monthly interest payment, and balloon interest and principal payment. In the asset side, they we re supposed to specialize in lending to a few sectors, but over the years, they have progressively overlapped each other so that the distinctions between them have been reduced to a minimum.

Like state banks, private national commercial banks raise funds by issuing demand and time deposit liabilities. Although permitted to lend at any maturity, they tend to concentrate on the provision of short-term loans (usually six months or less). This is not unusual among private commercial banks in ASEAN countries. Private national commercial banks used to be classified into foreign exchange and non-foreign exchange banks. But under the October 1988 deregulation package (PACTO 27), non-foreign exchange banks may deal in foreign exchange if classified "sound" in 20 of the last 24 months and if their total assets are greater than Rp 100 billion.

Foreign banks have a wider array of sources of funds, such as demand, savings and time deposits as well as borrowings from international markets. They may also engage in currency swaps with Bank Indonesia, the central bank of Indonesia, or borrow in the interbank market for rupiah funds. Foreign banks' loans have been concentrated in the overdrafts and short-term facilities. Any investment loans they want to make need special permission from Bank Indonesia. Most of the multinational companies in Indonesia prefer to bank with them.

5 H.W. Arndt, "Financial System of Indonesia", *Savings and Development*, Vol. 11, No. 3 (1987), p. 306.

Together with more than 50 representative offices of foreign banks in Indonesia, foreign banks have been involved in one way or another in the negotiation of foreign loans and foreign direct investment.

Development banks consist of one State-owned bank, 27 development banks which are either directly owned by local authorities or jointly owned by local authorities and private sector, and one privately owned bank. These banks concentrate in investment loans, and medium and long-term loans. The State-owned development bank raises funds by accepting demand and time deposits, and borrowing from Bank Indonesia, the government, and foreign long-term sources of funds. The local development banks are allowed to issue time and savings deposits. They may also have refinancing arrangements with the State-owned development bank.

The savings banks include one State-owned bank and four privately owned banks. The State-owned savings bank mobilizes deposits through the post office network. These savings are used to meet the credit requirements of low-income sectors.

The Indonesian government has equity participation in several non-bank financial intermediaries. Interestingly, foreign institutions have minority participation in almost all of the 12 non-bank financial intermediaries. Cole and slade describe the activities of non-bank financial intermediaries as follows:

> they deal in foreign exchange, commercial paper, long-term stocks and bonds, SBIs and SBPUs, and CDs, as well as in many banking operations. They serve as "agents" for State-owned bank purchases of SBIs and as "market makers" in the SBI market.[6]

B. Malaysia

Table 3 shows the financial system of Malaysia. In terms of assets, the banking institutions have dominated the system.[7] The banking system consists of commercial banks, finance companies, merchant

6 D.C. Cole and B.F. Slade, "Development of Money Markets in Indonesia", unpublished, 1990, p. 25. SBI stands for Sertificat Bank Indonesia, a discount bill, which is a liability of Bank Indonesia. SBPU stands for Surat Berharga Pasar Uang, which is another instrument used in the open market operations of Bank Indonesia.

7 As of 14 August 1990, the exchange rate was M$2.70 per US$1.

banks, discount houses and a specialized commercial bank that offers commercial banking services based on Islamic principles. Participation of branches of foreign banks in the Malaysian banking system is quite substantial.

Commercial banks in Malaysia carry the usual commercial banking functions in both the liability and the asset sides. They are the only ones licensed as full trading and cheque-paying banks. They are also allowed to deal in foreign exchange and to offer a variety of fee-based services. They may invest in shares of public and private companies up to 50 per cent of their capital base. The most important restriction in their liability side is that they are not allowed to accept deposits of less than one-month maturity.

Finance companies cater to the medium and long-term markets. They are allowed to accept savings and fixed deposits of three-month maturity or more but are not allowed to demand deposits. They are not permitted to deal in foreign exchange nor grant loans in the form of overdrafts. Their loans are mostly of long-term maturity.

Merchant banks operate in both the capital and money markets. In the capital markets, they provide underwriting facilities, corporate financing, financial investment, management advice and portfolio investment management. In the money markets, they engage in the trading of money-market instruments. Merchant banks are allowed to accept only large term deposits from financial institutions (not less than M$250,000 per deposit), corporations (not less than M$1 million per deposit), and foreign currency deposits from non-residents (not less than M$250,000 per deposit).

Discount houses operate mainly in the money markets. They are permitted to accept funds at call or short-term deposits of up to 3 months with a minimum denomination of M$50,000 from financial institutions, corporations, Federal, State, and local governments. Thus, they provide those with temporary surplus funds with an alternative investment outlet. The funds they raise are mainly invested in government securities. They are not allowed to lend to the public.

C. The Philippines

The structure of the Philippine financial system is not entirely different from those in other ASEAN countries. The financial institutions may be grouped into banking and non-banking financial institutions, with the former dominating the system in terms of assets (see table 4).[8] Government presence in both categories is substantial. Foreign participation in the banking system is also significant. Like the rest of the ASEAN countries, the Philippines is also moving towards universal banking and the reduction in the differentiation among different types of bank categories. Table 5 gives a summary of the authorized activities of various bank categories in the Philippines. Leasing is the only activity that is absolutely not allowed to universal and ordinary commercial banks. On the other hand, other types of banks may now obtain authority to perform functions that used to be reserved only to commercial banks provided they meet certain criteria, like minimum capital requirement.

The Philippines has an offshore banking system which is patterned after Singapore's. There were 21 offshore banking units (OBUs) as of December 1988 with total assets of $2.7 billion. This does not compare with those in Singapore. OBUs may use any currency, except domestic currency, in their transactions. Thus, they do not have swap facilities. They cannot accept deposits in foreign currency of less than $50,000. The purpose of establishing OBUs was to increase local residents' access to foreign currency funds. This may have been attained as suggested by the data in table 6, which shows that most of the funds of OBUs were lent onshore.

Recently, the Philippine commercial banks have been very active in their off-balance sheet activities. These are activities that generate income for banks without expanding the asset portion of their standard balance sheet. These activities have registered phenomenal growth among universal and commercial banks.

8 As of 14 August 1990, the exchange rate was P24.20 per $1.

D. Singapore

Singapore has the largest and most sophisticated financial system in the ASEAN region. It is considered as the fifth largest foreign exchange centre in the world today.[9] Its financial system consists of commercial banks, merchant banks, finance companies, national savings bank, discount houses and international money brokers (see tables 7 and 8).[10] Given its highly open policy and liberal exchange rate policy, the number of foreign banks increased tremendously and have made a very significant contribution to its financial system. All commercial banks may obtain from the monetary authorities an authority to transact in the Asian Dollar Market. They are however distinguished by the extent of their domestic banking business permitted by the monetary authorities. Both foreign and local *full license banks* are authorized to engage in the entire range of domestic banking business. *Restricted license banks* can perform domestic banking functions, but they are not permitted to accept savings and fixed deposits below S $250,000 from the non-bank public. The *offshore license banks* are authorized to engage in any transactions with non-residents except that they cannot accept deposits in any currency or fixed deposits below S$250,000. Also, they are not allowed to accept any interest bearing deposits from resident non-bank customers nor lend to them in excess of S $50 million.[11] This has made offshore banks in Singapore regionally and internationally oriented.[12] This is supported by the data in table 9. The shares of the items "amount due to and from banks" are significantly high in the case of commercial banks with Asian Currency Units.

Merchant banks in Singapore are similar in nature to the merchant banks of Malaysia. They are active in both the money and capital markets. They are not permitted to accept deposits from the public.

9 M. Ariff, B. Kapur and A. Tyabji, "Money Market Study: Singapore", unpublished, 1990.

10 Discount houses were discontinued in 1986. As of 14 August 1990, the exchange rate was S$1.80 per US$1.

11 Amina Tyabji, "Financial Reform in ASEAN", unpublished, 1989.

12 In contrast, the Philippine offshore banks have been made domestically oriented.

But they may source funds from the bank and may participate in the foreign exchange market with the approval of the monetary authorities. The data in table 8 suggest that merchant banks in Singapore are significantly active participants in the Asian Dollar Market.

Finance companies in Singapore have limited banking functions. Although they are permitted to accept savings and time deposits and grant loans to bank and non-banking entities, they do not have current account facilities. Also, they cannot deal in gold and foreign currency.

The Post Office Savings Bank (POSB), a government-owned savings institution, is very much active in the deposit market. It has 137 branches. It has current accounts and savings-deposit facilities. It is not however permitted to accept corporate deposits, finance foreign trade and engage in foreign exchange transactions. It may lend to banking and non-banking institutions. Lately, it has become a significant player in the money market of Singapore.

E. Thailand

Table 10 shows the financial system in Thailand. Like other ASEAN countries, the banking system has dominated the financial system in terms of assets.[13] Its banking system is composed of 30 commercial banks, of which 16 are domestic and 14 are branches of foreign banks, and 3 specialized government-owned banks. Of the 16 domestic banks, only one bank (the second largest bank) is owned by the Thai government.

The activities of the six types of financial institutions in Thailand are summarized in table 11. Commercial banks mobilize funds by accepting demand, savings, and time deposits, and by borrowing from domestic and foreign sources. Lending in the form of overdrafts used to be popular among commercial banks in Thailand.[14] In the recent past, however, loans and bills discounted have increasingly become important activities of commercial banks. Recently, commercial banks have been permitted to deal in foreign exchange and undertake several fee-based activities, such as loan syndication, consultancy service for

13 As of 14 August 1990, the exchange rate was Baht 25.57 per $1.

14 Note that overdrafts are not allowed anymore in the Philippines.

merger and acquisition, issuing credit cards, issuing letters of credit, bill collecting for government agencies, etc. Local corporate underwriting, stock broking, leasing, trust business, and management of provident funds are not allowed to them. The share of income from fee-based services in the total income of commercial banks has significantly increased from 5.6 per cent in 1983 to 10 per cent in 1987. Thailand still maintains ceilings on interest rate on loans and deposits.

We must underscore at this point the increasing internationalization of banking in the ASEAN region. It comes in two forms. One is the extent of participation of foreign banks in the financial system of ASEAN countries; and the other, the extent of participation of ASEAN banks in international banking. The substantial physical presence of branches of foreign banks in all ASEAN countries has already been noted above. This does not include the numerous representative offices of foreign banks in the ASEAN countries. There are more than 50 of them in Indonesia, 26 in Malaysia, 19 in the Philippines, 47 in Singapore, and 37 in Thailand. The combined assets of branches of foreign banks range from 4 to 8 per cent of the total assets of the financial systems in Thailand, Indonesia, Malaysia and the Philippines. This obviously understates the extent of participation of foreign banks in the financial system of these countries since aside from directly mobilizing deposits and lending to banks and non-bank enterprises, they also constitute important links between the ASEAN countries and international financial markets. In Singapore, the total assets of foreign (full and restricted license) and offshore banks accounted for 92 per cent of the total assets of its commercial banking system in 1988.[15] Although the Philippines has the lowest number of branches of foreign banks, 10 out of its 24 domestic universal/commercial banks have substantial foreign equity participation.

ASEAN banks have also participated in international banking. As shown in table 12, ASEAN banks have a significant number of branches and subsidiaries in the Pacific region. This has shown to be increasing between the mid-1970s and 1983 at least for some large banks (see table 13). At present, the 13 local full license banks of Singapore have a large network of overseas offices that include 96 branches, 8

15 See table 2.3 of Ariff, et al., *op. cit.*

agencies, and 16 representative offices. The Thai local banks have 22 branches overseas. The Philippines have 14 branches, 2 agencies, and 8 representative offices overseas. The record of intra-ASEAN exchange of banking facilities is not that impressive, however. There is more interaction between Malaysia and Singapore than the rest of ASEAN countries because of their strong historical ties (see table 14). One encouraging note though is that except for Brunei, an ASEAN member country has at least one branch bank in another member country.

ASEAN banks appear to be active participants in the international interbank market. Indonesia, Malaysia and Thailand were net lenders in this market, whereas the Philippines and Singapore were net borrowers. Their net positions have improved between 1983 and 1988. In cross-border transactions from ASEAN banks to non-bank institutions, only Singapore showed significant amount of activity. This was largely due to the presence of its internationally oriented offshore banking system. On the deposit side, again Singapore figured prominently. Philippines, which has an offshore banking system that is concentrating on raising funds, is a distant second.

II. STRUCTURES OF MARKETS AND COMPETITION

This section examines the structures of markets and competition of the ASEAN banking systems. In this regard, we look at certain indicators, such as structure of ownership, policy on bank entry and branching, degree of concentration, and pricing.

A. Structure of ownership

In this aspect, we focus on the relative share of government and the private sector in the ownership of financial institutions. It should be pointed out at the outset that a government-run financial institution does not necessarily need to be inefficient. It could be as efficiently managed as the privately run financial institution. However, if it is being conferred with special privileges and subsidies, then it would be very hard for private financial institutions operating in the same market to compete with it. An example is that a government bank is made the sole depository financial institution of all government-owned corporations. Access to cheap funds will allow itself to price its loans at be-

low market rates. Even in the absence of special privileges and subsidies, being a government bank already confers certain advantages. This is particularly true in countries where there is no deposit-insurance scheme and where the financial system is highly unstable.

Governments in ASEAN countries are not only involved in regulating financial institutions, but also directly participating in the provision of financial services through State-owned financial institutions. However, the degree of their involvement and their impact on the financial markets differ from country to country. In Indonesia, the government has substantial equity participation in practically all key financial institutions. It owns the five largest commercial banks with numerous branches nation-wide, the largest development bank, the largest savings bank, the largest non-bank financial institution (NBFI) plus substantial equity participation in practically all NBFI, and the sole pawnshop with more than 400 branches all over the country. As Cole and Slade pointed out:[16]

> State-owned banks have paid lower interest rates on deposits that private banks throughout the period, but as there is no deposit insurance in Indonesia, State-owned banks may have appeared "safer" to many depositors.

It was only after the October 1988 deregulation that State-owned banks ended their monopoly of deposits of public corporations. Erquiaga observed that "the state banks have come under increased scrutiny over the last several years because of perceived operational inefficiencies compared to the foreign banks and some of the national commercial banks."[17]

The direct participation of government in banking can also be seen in Malaysia. Government ownership of financial institutions is pronounced in both the banking and non-banking institutions. A recent study indicated that "the commercial banking system is dominated by two largely Government-owned commercial banks, accounting for 35.8 per cent of the total assets of all commercial banks as at the end of June 1989; their branch network of 327 offices represented more than

16 Cole and Slade, *op. cit*, p. 43.

17 Philip Erquiaga, "Improving Domestic Resource Mobilization through Financial Development: Indonesia", *ADB Staff Paper*, No. 40 (Manila, ADB, 1990), p. 55.

35 per cent of the total banking network.[18] However, these banks are considered to be efficiently managed. Both the privately owned domestic and foreign banks consider the financial market in Malaysia to be competitive. This is mainly attributed to the openness of its financial system.

In the Philippines, the government owns the largest universal bank, which has the most extensive branching network, and the largest development bank. Both of them suffered financial difficulty in the mid-1980s as a result of "behest loans" made by them during the previous regime. They were rehabilitated, but the government had to absorb their non-performing assets worth over P100 billion. The government-owned universal bank is now in the process of being privatized, with 30 per cent of its total outstanding shares already sold to the private sector. The government has still maintained the policy of requiring all government agencies and government-owned corporations to deposit their surplus funds only in government-owned banks.

Even Singapore which has a highly open financial system allows government participation in the banking system. However, its savings bank (POSB) is shown to be innovative and competitive, while the semi-governmental commercial bank (DBS) serves as a counterweight to the "Big Four" local banks so that its "presence has served to enhance the competitiveness of the banking system".[19]

Perhaps, Thailand differs from the rest of the ASEAN countries in this area. It has been noted that the Thai Government ownership and control of financial institutions and therefore the relative importance and number of specialized institutions are very small.[20]

As regards foreign ownership of banks, Singapore ranks first in terms of the number of foreign-owned banks operating domestically. Indonesia, Malaysia and Thailand have ten or more branches of foreign banks that do domestic banking, whereas the Philippines has only four.

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18 Lin, et al., *op. cit.*, p. 11.

19 Ariff, et al., *op. cit.*

20 Edita A. Tan, "Development Finance and State Banking: A Survey of Experience", *PIDS Staff Paper Series*, No. 84-04 (Makati, Philippine Institute for Development Studies, 1984), p. 45.

But it should be noted that foreign banks have minority participation in ten domestic banks in the Philippines.

B. Policy on bank entry and branching

This is one area where some ASEAN countries have made certain progress in the past few years to improve the competitiveness of their banking system. However, the degree of relaxation on bank entry significantly varies among ASEAN countries. In Indonesia, nationals may acquire a license to operate a bank anywhere in the country provided they meet the minimum-capital requirement. Foreign banks are encouraged to have joint ventures with Indonesian nationals. This privilege is available only to those that come from countries with reciprocal agreement with Indonesia. They may own up to 85 per cent of the outstanding equity shares of joint-venture banks. This is an improvement over minority share allowed for them before the PAKTO 27 (October 1988) reforms. However, they are restricted to only 7 major cities and are required that within 12 months, their outstanding export credits be at least 50 per cent of their total outstanding credits. In the meantime, no new branches of foreign banks are allowed. As regards branching, banks wholly owned by Indonesian nationals may open branches anywhere in the country, whereas existing foreign bank branches may open one sub-branch only in each of the 7 major cities. Branches of foreign banks do not have rediscounting privileges with the central bank of Indonesia.

Malaysia's policy on bank entry and branching remains the same. In particular, no new banks are allowed to enter the Malaysian financial system, and its policy toward foreign-bank operation does not encourage the establishment of more branches in the country. Opening of new branches is allowed only to local banks. Branches of foreign banks do not have rediscounting privileges with the central bank of Malaysia.

The Philippines has recently relaxed its policy on bank entry and branching. The Monetary Board has been processing some applications for bank entry that include equity participation by foreign banks. The present law allows foreign investors to own up to 30 per cent of the outstanding shares of a domestic bank. Entry by branches of foreign banks is still restricted. Instead, foreign banks are being encouraged to

establish offshore banks in the Philippines or buy equity shares of existing domestic banks. It seems that only Indonesia and the Philippines encourage joint-venture banks at present. Existing branches of foreign banks may open branches in other parts of the country but they are not allowed to accept demand deposits. This restriction has the same effect as the restriction on branching since demand deposit is a key service facility offered by branches of foreign banks. Like domestic banks, branches of foreign banks have rediscounting privileges with the central bank of the Philippines.

Thailand has not allowed new entrants into its commercial banking system for quite sometime already. Instead, local banks have been encouraged to open branches in rural areas. Branches of foreign banks are still prohibited from opening sub-branches anywhere in the country. Like local banks, they have rediscounting privileges with the central bank of Thailand.

C. Degree of banking concentration

We use here two measures of banking concentration - namely, the asset share of the five biggest banks to the total assets of banks in each country and the Herfindahl index. Only those domestic and branches of foreign banks belonging to the commercial banking system are included.

In both measures, it appears that Indonesia has the highest degree of banking concentration. The first five banks, which happen to be all State-owned banks, constitute 81 per cent of the total assets of the commercial banking system. Thailand follows Indonesia, with the five largest banks accounting for 68 per cent of the total assets of commercial bank assets. Thailand has the biggest commercial bank in the region with total assets amounting to about $17 billion. Philippines appears to have the lowest concentration ratio. This is because more than half of the assets of a government-owned commercial bank that were deemed non-performing had been recently transferred to the national government. In general, these findings suggest that a high degree of banking concentration exists in the four ASEAN countries.

D. Pricing

The structure of the market could be reflected in the spread between the cost of funds and the lending rate. An inefficient banking system characterized by greater concentration is likely to be associated with a larger bank spread. The Philippines, Thailand and Indonesia have on the average larger bank spreads than Malaysia and Singapore. It is however to be noted that the bank spreads for the Philippines, Indonesia and Thailand have declined in the past two years. The openness of the financial systems of Singapore and Malaysia could have acted as a strong pressure on bank spread. Malaysia and Singapore are even found to have lower average bank spreads than Japan and Germany.[21]

The larger bank spreads observed for the Philippines, Thailand and Indonesia cannot be wholly attributed to the kind of market structures existing in these countries. Regulatory measures, such as those pertaining to intermediation taxes (e.g. high reserve requirements, mandatory credit allocations to certain priority sectors, etc.) could also be contributory to the large bank spread.[22] The available evidence, at least for the Philippines and Thailand, seem to support this. For Thailand, the cost of the said regulations comprises about 30 per cent

21 Ariff, et al., *op. cit.* have pointed out that the openness of the financial system of Singapore "serves to place a limit on the permissible width of spreads." (p. 26). Also it "is generally believed that the DBS' presence has served to enhance the competitiveness of the banking system, in terms of a narrowing of the spread between lending and deposit rates" (p. 29). DBS is a semi-government bank that intensely competes with the private banks.

22 In the Philippines, all banks are required to allocate at least 25 per cent of their total loanable funds to the agricultural sector. In Thailand, commercial banks must extend credits for the purpose of rural development in the amount of at least 20 per cent of deposit liabilities as of the end of the previous year. In Indonesia, national banks are required to allocate a minimum of 20 per cent of loan portfolio to small business. These are examples of mandatory credit allocations. Mandatory credit allocations could lead to the widening of bank spread. In the Philippines, for example, banks that do not wish to lend to the agricultural sector may buy government securities as a substitute for their compliance of the regulation that they allocate 25 per cent of their total loanable funds to the said sector. The interest rate on government securities eligible for such purpose is fixed at a level substantially below the prevailing lending rates (and at times, even below the deposit rate). Banks recover their losses here by passing them on to borrowers in terms of higher lending rates.

of commercial banks' spread between lending and deposit rates.[23] Thus, intermediation taxes aggravate the plight of borrowers in a less competitive financial system.

III. BENEFITS AND COSTS OF A MORE LIBERAL REGIME FOR INTERNATIONAL TRADE IN BANKING SERVICES IN THE ASEAN REGION

This section discusses the benefits and costs of a more liberal regime for international trade in banking services in the ASEAN region. There are two aspects of internationalization of finance - namely, cross-border and establishment-related trade in financial services. This paper focuses on the latter. Establishment-related trade in banking services refers to "services produced by factors of production whose ownership resides in one country and sold to residents of another through some form of direct presence of the supplier in the client's country."[24]

A. Benefits

There are benefits to a more liberal regime for international trade in banking services in the ASEAN region. First, it improves access of the population to banking services in general. It has been shown above that except for Singapore, ASEAN countries are still generally underbanked. Also, the distribution of bank services is badly skewed in favour of the capital city (i.e. Metro Manila for the Philippines, Bangkok for Thailand, and Jakarta for Indonesia). The recent liberalization on bank entry and branching in most ASEAN countries is indeed a welcome development. It could perhaps be extended to branches of foreign banks. But their contribution to banking development in the country is likely to be limited if they are confined to locate only in the capital city of the country concerned. As already pointed out above, all ASEAN countries have already several branches of foreign banks located and operating in capital cities. Thus, allowing new entrants or

23 TDRI, 1987 Year-End Conference on Efficiency and Competitiveness of Thai Economy, unpublished, November 1987.

24 GATT document MTN.GNS/W/68, 4 September 1989, p. 6.

branch networks of foreign banks in other places within the country would be more desirable than having new branches of foreign banks situated in a capital city. Indonesia is already moving in this direction, although it is initially limiting this privilege to existing branches of foreign banks.

Second, it encourages foreign investors to locate themselves in areas other than the capital cities of ASEAN countries. This augurs well for a more balanced regional development within a country which has been the obsession of policymakers for decades. It is to be noted that in the past decade, ASEAN countries have heavily invested in infrastructural development in certain regions within their territories to induce foreign investors to locate themselves in those areas. The immediate availability of services from international banks with which they have long-established relationship will further strengthen their decision to locate in those areas because aside from ordinary banking services, they may also require from their preferred banks ancillary banking services, such as payroll services, portfolio investment, etc. The delivery of such services requires the physical presence of their banks in the area.

Third, increased competition in the banking system can be extended to other regions or areas of the country with the presence of foreign banks in those areas. Thus, more people will be exposed to a wider set of financial instruments with more attractive rates of returns. So far, foreign banks' competition with domestic banks has been confined to the capital city of the country, benefiting only wealthier residents. This is so because of the host government's policy of disallowing branches of foreign banks to open sub-branches in other parts of the country.

And lastly, improvements in intra-ASEAN trade and investment, which ASEAN countries have been diligently working on as may be observed from the various activities that have already been done and are being lined up for this purpose, would require better banking infrastructure, and such could be achieved through a more liberal regime for regional and international trade in banking services. The competitiveness of ASEAN banks that would result from a more liberal financial system at home will prepare them to participate in regional

and international banking. Indeed, the experience of Singapore in this area is worth considering.

B. Costs

Any undertaking always involves some costs that must be weighed against the benefits. The move towards a more liberal regime for international trade in banking services has some costs. Deregulation might breed excessive risk-taking among competitors. This is worse in a country where there is a compulsory deposit-insurance scheme because of the moral-hazard problem that it may generate. The Philippines is a case in point. However, even in those countries where no deposit-insurance scheme exists, the policy of bailing out any ailing bank could be considered by market participants as a form of insurance. Thailand could serve as an example here. In both cases, the government concerned will have to bear the burden of those losses. Of course, the other alternative is to allow bank failures and to let the participants absorb all the costs. But it generates another cost, i.e. it undermines the people's confidence in the banking system, which might turn out to be more costly in the long run. This only serves to underscore the importance of having a strong and efficient supervisory organization as well as effective prudential regulations in ASEAN countries. This, too, involves additional costs since supervisory staff have to be trained and paid well.

During the heyday of low interest rate in the international market, several countries refused to make adjustment to correct their worsening current-account imbalances since cheap funds were readily available from the international market to finance such deficits. The Philippines was one of them.[25] With a more liberal regime for international trade in banking services, the inflow of foreign capital that might be facilitated by branches of foreign banks could hide any imbalances in the current account.[26]

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25 Mario B. Lamberte, et al., *A Review and Appraisal of the Government Response to the 1983-84 Balance-of-Payments Crisis* (Manila, PIDS, 1985).

26 See Kazumasa Iwata, "Liberalization of Trade in Financial Services", in Leslie V. Castle and Christopher Findlay, *Pacific Trade in Services* (Sydney, Allen and Unwin, 1988). The literature on the order of economic liberalization provides ample lessons for this. See, for example, Sebastian Edwards, "The order of liberalization of External Sector: An Analysis Based on the Southern Cone

Finally, the present superiority of foreign banks over domestic banks in technology-based transactions, which most banking services are now, could result in undue competition.[27] Monetary authorities may end up supervising more foreign banks than domestic banks. Apart from supervisory problem that may arise from this, the effectiveness of monetary policy could be undermined. This could be one of the reasons why ASEAN countries prefer to promote joint ventures than allow new branches of foreign banks to enter the domestic financial system.

It is our view that the benefits that will be derived from a more liberal regime for international trade in banking services in ASEAN countries outweigh the costs. However, liberalization should be carried out gradually and should be in step with the development of the economy. The timing of the liberalization is also important.

IV. THE APPLICABILITY AND IMPLICATIONS OF THE URUGUAY ROUND KEY CONCEPTS, PRINCIPLES AND RULES

This section discusses the applicability and implications of the key concepts and principles discussed in the multilateral negotiations on trade in services to the banking sector in the ASEAN countries. In this regard, Cornford's comments on the proposals of the European Community and United States in the Uruguay Round negotiations on trade in services concerning an agreement regarding international trade in financial services are very relevant.[28]

Before we proceed with the assessment of the applicability and implications of the concepts, principles and rules, it would be useful to

Experience", University of California, Los Angeles, Department of Economics, 1985. See also Vittorio Corbo and Jaime de Melo, "Lessons from the Southern Cone Policy Reforms", *The World Bank Research Observer*, Vol. 2, No. 2 (July 1987).

27 This could arise from economies of scale. For instance, a multinational bank may develop its own computer software for market analysis that can be used by its branches all over the world.

28 Andrew J. Cornford, "Comments on the Proposals of the European Community and the United States Concerning an Agreement Regarding International Trade in Financial Services", unpublished, 1990.

comment briefly on the specific characteristics of the financial sector which might call for sectoral annotation to the multilateral framework agreement for banking services. The service sector in general is a group of heterogeneous economic activities. Each sub-sector also consists of finer groupings of economic activities. But the banking sector clearly stands out from the other sub-sectors in the services sector. Its function in the economy is unquestionably large. A significant portion of the trade in goods and services, both domestic and international, passes through the banking system. A dysfunctional banking system can certainly impair trade. Aside from this, the banking system also provides portfolio investment services to customers. In most of these transactions, the physical presence of banks near their clients is very important.

Monetary policy is transmitted to the rest of the economy through the banking system. Thus, there is a strong motivation for monetary authorities to maintain a properly-functioning banking system. It is understandable that the banking sector is one of the highly regulated sectors in the economy. This is ostensibly to preserve the payments system and to protect consumers so that their confidence in the banking system is maintained.

The banking sector has been experiencing rapid innovations especially with the advancement in communications and computer. This may be gathered from the variety of financial services and instruments that are currently available in the market. With the further deregulation of the financial markets in both developed and developing economies, financial institutions will certainly be busier in developing more financial services and instruments. Thus, both the wholesale and retail markets for financial services will become more complex and sophisticated than what they are already now.

A framework agreement that is applicable to all service sectors is highly desirable. However, if it is expressed in a very general manner and does not address the specificities of the banking sector, it is likely to lead to more disputes could impair the usefulness of the agreement. Thus, a sectoral annotation to the multilateral framework could address the specificities of the banking sector so that resort to dispute settlement procedures will be minimized.

A. Transparency

It is not uncommon to see various branches of the governments of ASEAN countries involved in promoting, regulating and supervising the same business entities. Each one of them issues specific guidelines that are not usually well circulated. Neither are these activities well co-ordinated. Going through the exercise of knowing what guidelines apply and where to obtain them already entails much effort and money for local residents. For foreigners, this is almost impossible, especially if those guidelines are written in local languages. Thus, for ASEAN countries, there is a need to consolidate all those regulations and guidelines pertaining to banking laws, in general, and to laws covering trade in banking services, in particular. Each country may assign an office which can serve as a "one-stop shop" for all those laws, regulations and guidelines affecting trade in banking services. This may be patterned after the "one-stop shop" for the export sector that all ASEAN countries have, although in a limited scale. It is preferable that this office be housed at the Central Bank. All government agencies should be required to submit to this office all laws, regulations and guidelines, and any amendments thereof, that have some effects on banking operations. All inquiries pertaining to specific laws or guidelines in banking, either from own citizens or foreigners, will be addressed to it. All branches of foreign banks should likewise be required to submit to this office any information about their operations.

At the ASEAN level, the Committee on Finance and Banking (COFAB) may serve as a "one-stop shop" by consolidating what each member had already done. Thus, any interested third party does not have to contact each individual country office if he wants to make inquiries about banking laws, regulations and guidelines from all the ASEAN member countries.

B. Progressive liberalization

As already pointed out above, ASEAN countries are now in different stages of financial liberalization. Leading the pack in this effort is Singapore, followed by Malaysia. The remaining ASEAN countries have now gradually shifted their attention from credit allocation to the general soundness and stability of the financial system. The need for

strong and efficient supervision is clearly felt in these countries. Since such supervision takes time to develop, ASEAN countries should opt for a gradual but progressive liberalization process. This has been the path followed by Singapore.

The changing role of existing branches of foreign banks in the ASEAN region must also be recognized. In the past, they had been heavily involved in the financing of imports of multinational companies, most of which were established during the import-substitution regime of these countries, and in packaging sovereign loans. As noted in Section I of this paper, their business for the latter had substantially declined as a result of the international debt crisis. At the same time, ASEAN countries that used to be inward looking have now switched towards export-orientation and more industrial dispersal of industries. Thus, there is increasing activity in this area in which branches of foreign banks are not able to participate due to existing regulations, such as prohibition against opening branches outside the capital cities. This still exists today despite the fact that ASEAN countries, except Singapore, are generally "underbanked." Thus, there seems to be some scope for allowing foreign banks to be included in ASEAN countries' on-going financial liberalization.

Since the presence of branches of foreign banks operating in the capital cities of ASEAN countries is already substantial, sub-branches of foreign banks may be opened in areas outside the capital cities. This will extend the competition between foreign and local banks in the countryside, and at the same time, surplus units and foreign investors who locate themselves in the countryside will be offered a wider menu of banking services. This may be accompanied with the promotion of joint ventures. Although most ASEAN countries have already maintained such policy, the extent of equity participation by foreign banks in joint ventures may be increased.

C. Market access

ASEAN countries have been exercising control over market access to their financial systems to pursue certain objectives, such as maintaining the stability of the financial system and effectiveness of monetary policy, configuring the structure of their financial systems to

meet the changing needs of the economy, developing banking skills of local professionals, etc. As is currently envisaged, the framework agreement will provide the market access and national treatment are the subject of specific concessions at the sectoral and sub-sectoral level. This should allow ASEAN countries to exercise a certain flexibility so that they can continue to pursue those objectives while they proceed with their financial liberalization. In this regard, certain aspects of the financial systems of ASEAN countries must be considered. One is the substantial presence of foreign banks in ASEAN countries in the form of branches, joint ventures, agencies and representative offices. This serves as a testimony that they recognize that commercial presence of foreign financial institutions in various forms is important for the delivery of financial services. However, conceding market access automatically to all signatories at this time may not be advantageous to ASEAN countries since, given the substantial presence of foreign banks in these countries, it could easily lead to a situation wherein foreign banks dominate their financial systems. A quota system wherein ASEAN countries determine the number of additional foreign banks they will permit to have commercial presence in their markets may be necessary. This may be applied to all forms of commercial presence of foreign banks, except in the case of joint ventures provided that nationals retain control over the financial institutions. The quota system should be applied in a non- discriminatory manner.

Another aspect is the trend towards universal banking or the blurring of distinctions among different types of financial institutions. It should be noted that ASEAN countries are gradually moving, though at different speeds, toward this direction. Thus, in the long run, the use of market access to develop or improve the efficiency of particular sub-markets may not be relevant anymore. In the short run, however, the use of market access for such purposes is still relevant. One reason is that regulations that distinguish different types of financial institutions still exist. Another reason is that some sub-markets of the ASEAN financial systems are not yet well developed and that there are no operative prudential regulations covering those markets. Thus, at this stage of the development of the ASEAN financial systems market access should be conceded on a sub-sectoral rather than universal basis.

D. National treatment

The Mid-Term Review decision states that "when accorded in conformity with other provisions of the multi-lateral framework, it is understood that national treatment means that the services exports and/or exporters of any signatory are accorded in the market of any other signatory, in respect of all laws, regulations and administrative practices, treatment 'no less favourable' than that accorded domestic services or services providers in the same market."[29] This has substantial impact on the current policy of ASEAN countries on branches of foreign banks, but less on joint ventures and other forms of commercial presence of foreign banks. The typical forms of discrimination exercised by ASEAN countries against foreign banks include the following: ban on the establishment of branches; limit on the range of banking services they can offer, such as trust business; no access to refinancing facilities; and prohibition against purchasing local properties for business purposes.[30] Of course, the degree of restrictiveness varies across ASEAN countries. Given that most areas outside the capital cities of ASEAN countries are still underbanked, the changing pattern of the business of branches of foreign banks, and the export-orientedness of ASEAN countries, there seems to be a good reason for including foreign banks in the branching deregulation currently being undertaken by ASEAN countries. As regards the range of services that may be offered by branches of foreign banks, this may be gradually liberalized in step with the move towards universal banking.

It might be appropriate at this point to comment on the proposals of the EC and the United States on market access and national treatment, since both proposals seem to link market access to national treatment very closely.[31] Cornford's distinction between the issues under market access and those under national treatment should be subscribed to by ASEAN countries. As regards market access, the United States proposal which also reflects that of the EC proposal states that:

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29 "Uruguay Round Mid-Term Review", in UNCTAD, *Trade in Services* (United Nations Publication, UNCTAD/ITP/26), p. 481.

30 These are mentioned Seiji Naya, et al., *ASEAN-US Initiative: Assessment and Recommendations for Improved Economic Relations* (Singapore, Institute of South-East Asian Studies, 1989). They have also been indicated in the discussion in the previous sections.

31 Cornford, *op. cit.*

"Each party (a) shall permit financial service providers of another Party to establish or expand an enterprise for the provision of a financial service, and (b) shall permit such enterprises to provide financial services and to conduct activities associated with the provision of financial services." This is going far beyond what ASEAN countries can possibly offer. As regards (a), ASEAN countries will be obliged to open their markets to all signatories. As already mentioned above, foreign banks can easily overwhelm the market since there is already a substantial number of foreign banks currently operating in various forms in ASEAN financial markets. It may well be for ASEAN countries to resort to a quota system if they think that additional foreign banks can be accommodated by the financial system. What may be conceded by ASEAN countries is the relaxation of the prohibition against foreign banks to expand their business through branching within each ASEAN countries' territory for reasons already cited above. As regards part (b), it obliges ASEAN countries to grant universal license to foreign service providers while such license is selectively given to domestic financial institutions. Even universal banks in ASEAN countries are not permitted to provide all the financial services mentioned in the United States and EC proposals. For instance, financial leasing is not allowed to existing ASEAN universal banks. Also, there are financial services mentioned in both proposals that are not yet well-developed in ASEAN countries, hence there are virtually no regulations covering them. Once developed or fully appreciated by ASEAN countries, there might be a need to introduce new regulations for prudential reasons that might include restricting the benefits already enjoyed by financial services providers of other parties. Under Article 7.2 of the EC proposal, this could not be done anymore once signatories agree to their proposal.

As regards national treatment, both the EC and the United States proposals are concerned more about the *results* of having a competitive environment than on the policy of promoting competition *per se* in the markets. Cornford is right in his observation that "equality of competitive opportunity" seems an untried but potentially more intrusive obligation than like treatment as regards taxation and regulation.[32] New entrants may be in a disadvantageous position

32 *Ibid.*

compared with those that have been in the market for a long time, and some of them may not survive under an environment of stiff competition. This situation may be interpreted as not promoting "equality of competitive opportunity." Since the results seem to be unfavourable to certain parties, although the policy environment promotes competition. Another example can be cited, where the results of having a competitive environment can be distinguished from the policy of promoting competition *per se* in markets. As already mentioned above, ASEAN countries, except Singapore, still maintain loan portfolio allocation policy because they expect their banking system to perform developmental functions in addition to commercial functions. They require banks to lend to priority sectors, such as agriculture and small and medium industries. Even if such policy is applied equally to all banks in their territories, foreign banks may be placed in a disadvantageous position because of their unfamiliarity with the sectors and probably because of the relatively higher transaction cost they incur for granting small loans when their operations are designed for the wholesale market. Again, this could be interpreted as not promoting "equality of opportunity". To deal with this issue, the United States proposal recommends the provision that "No party shall establish or maintain any measure that requires that financial service be provided by financial service providers of that Party." While many analysts would like to see this being done, it might take ASEAN countries some time to dismantle their credit-allocation policy given the circumstances under which they were introduced and maintained.

E. Most favoured nation/Non-discrimination

Under this concept, all signatories will guarantee that concessions made by one party would be equally accorded to all. This concept, in its purest form, may lead to unlimited entry by foreign financial services providers into ASEAN countries' financial markets when access has been granted. This is more problematic for those countries that do not yet have efficient supervisory institutions and prudential regulations. The quota system mentioned earlier would come into conflict with the MFN principle. However, the scales and modalities for ensuring that the quotas were applied in the least discriminatory manner, would be laid out in a sectoral annotation. At this point, it might be important for ASEAN countries to stress the need for spreading the representation

of banks among geographical areas for promoting and diversifying trade and investment. As regards opening the financial markets, ASEAN countries may adopt an approach to phased liberalization though including additional sub-sectors, and enlarging quotas consistent with the level of financial development of each country. Thus, the speed of liberalization in all or some sub-sectors of the financial system may be different among parties - faster for countries with more developed financial systems and slower for countries with less developed financial systems. ASEAN countries should ensure that they will retain greater flexibility in opening up their financial markets in the future rounds.

F. Increasing participation of developing countries

As already mentioned above, ASEAN banking systems are already participating in international banking, although still in a small way. This can further be increased if ASEAN countries successfully hurdle at least two obstacles. One is the strengthening of their financial system, in general, and the individual financial institutions in particular. This hinges on a number of factors, such as improvement in their prudential regulations, availability of skilled manpower, adequate computer and communication facilities, etc. Joint ventures with foreign banks and the requirement to hire local professionals in important positions of foreign banks could be one of the ways to deal with the problem of lack of banking expertise in ASEAN countries. More competitive banks at home managed by professional bankers can easily integrate themselves in the international banking community. This should be taken into consideration in the liberalization process because premature or indiscriminate liberalization could lead to greater concentration of the ASEAN financial markets in foreign hands. Under this situation, there will be no ASEAN bank to speak of that could participate in international banking.

The second obstacle that ASEAN countries must hurdle is that of increasing their trade and investment. ASEAN banks could follow the business of their nationals in other countries. The volume of business should reach a certain level that can sustain the initial operations of ASEAN banks in those countries. As banking business expands, branches/subsidiaries of ASEAN banks can perhaps start extending banking services to nationals of host countries. This is a long shot for

ASEAN countries, and it greatly depends on how their export of goods and capital are treated in host countries.

G. Regulatory situation

The Montreal document is very much relevant to ASEAN countries in this aspect. It recognizes the right of countries to introduce new regulations. Regulations are needed even in the process of liberalization to finetune the financial system so that the effectiveness of monetary policies shall be maintained. As already noted above, some of the banking institutions and banking activities may be new to the ASEAN banking systems, hence prudential regulations are needed in order to maintain the integrity of the financial system as well as to protect depositors and investors. Some ASEAN countries are in the process of reorganizing their regulatory bodies. In the Philippines, for example, there are a number of bills that seek to reform the key regulatory bodies, such as the Central Bank, and the Philippine Deposit Insurance Corporation. There is also an attempt to reform the Securities and Exchange Commission in order to make it the lead agency in the capital market. Thailand and Indonesia are not far behind in this process.

The EC and the United States seem to have different views in this area. The EC proposal allows new regulations that may be introduced after the agreement only to "prevent or solve a serious economic crisis or financial disturbance." As already mentioned above, ASEAN countries may introduce new regulations especially in newly developed financial sub-markets for prudential reasons, even if there is no imminent crisis. In contrast, the United States proposal accommodates new regulations after the agreement for prudential reasons, but it adds that "such actions shall not prevent the establishment by financial service provider of another Party of an enterprise for the provision of financial services on conditions which accord national treatment." It should be pointed out that the new regulations could include limiting the number of players in newly established sub-markets in order to control the level of competition in those particular sub-markets.

H. Safeguards and exceptions

The framework agreement should include safeguards to allow ASEAN countries to operate with some flexibility. In the event of severe balance-of-payments crisis, ASEAN countries may temporarily suspend the liberalization process committed under the framework agreement while they sort out the causes of the problem. They may resort to discriminatory measures if there is sufficient evidence to show that the imbalances were caused by excessive activities of foreign financial services providers in host countries. This is in sharp contrast to the United States (article 8) and EC (article 15) proposals. Safeguards are also necessary to prevent foreign financial services suppliers from practising predatory pricing in host countries.

V. INCREASING COMPETITIVENESS OF BANKS IN ASEAN COUNTRIES AND INCREASING THEIR SHARE OF INTERNATIONAL TRADE IN BANKING SERVICES

This section examines some measures that can improve the competitiveness of ASEAN banks and increase their share in international trade in banking services.

A. Improving competitiveness

ASEAN countries have already identified some barriers to competition among banks operating within their own territories. Indeed, there are serious efforts to dismantle these barriers. One of these barriers is the presence of several large State-owned financial institutions in the ASEAN financial markets. The special privileges they enjoy confer them undue advantage over private banks. Although originally designed to be development banks, State-owned banks have gradually moved into areas where private banks are operating. There is now a move towards privatizing most of these State-owned banks while the special privileges given to the remaining ones have been slowly phased out. This process could perhaps be accelerated.

The selective credit-control policy of ASEAN countries has undermined the competitiveness of ASEAN banks. It has weakened the initiative of bank managers to manage loan portfolio since a big chunk of it is earmarked to specific priority sectors. The dismantling of this policy, which was already begun by some ASEAN countries, will hopefully develop more professional bankers in the region.

In the past, policies that encouraged specialization have fragmented the financial markets of ASEAN countries and reduced competition among different types of financial institutions. The recent trend towards universal banking will hopefully increase competition among different types of financial institutions. Fee-based activities have been encouraged. This is important since there is a growing market for fee-based services for both domestic and foreign clients. Experience of ASEAN banks in this area will be extremely useful when they compete in the international financial markets.

Prudential regulations in ASEAN countries have also been revised to reduce instability in their financial systems that might result from stiffer competition. For instance, capital requirements for practically all types of bank categories have been revised upwards. This will encourage small banks to merge among themselves or accept foreign equity participation. Also, rules on loans to bank directors, officers and related interests have been tightened to discourage them from committing fraud. A strong bank that has a good track record at home will be in a better position to enter the international banking community.

Finally, a policy of allowing branches of foreign banks to expand their operations within the territories through sub-branching and to diversify their banking services can further enhance the competitiveness of ASEAN banks. Branches of foreign banks operating in ASEAN countries have served as an impetus for competition. Moreover, they are key sources of banking innovations. This is important to ASEAN countries since there are no patents to innovative banking instruments and services developed by foreign banks.

B. Increasing the share of international trade in banking services

One of the ways by which ASEAN banks can increase their share of international trade in banking services is through the integration of their financial markets. This, of course, requires harmonization of their banking policies. It might be worthwhile to consider this at this moment since ASEAN countries are in the process of liberalizing their financial markets. Joint-venture banks could be easily encouraged among ASEAN countries if their banking regulations and tax systems are harmonized.

There are already some initiatives being made by ASEAN countries to expand intra-ASEAN banking activities. These initiatives need to be encouraged further. One such measure is the agreement on using ASEAN currencies in intra-ASEAN trade. It will promote the expansion of trade particularly with these ASEAN countries which are confronted with chronic balance-of-payments deficits or whose traders are covered by tight foreign-exchange regulations. More importantly, it will expand intra-ASEAN banking activity arising from greater intra-ASEAN financial flows.

Another initiative, which unfortunately has not yet taken off the ground, is the development of the ASEAN bankers' acceptance (ABA). It is supposed to capture the ASEAN markets on acceptances which have been largely serviced by American and British banks. The ABAs would be eligible only to cover imports of goods from other ASEAN countries. With harmonization of banking regulations and tax system as well as relaxation of foreign exchange regulations among ASEAN countries, progress in the development of ABAs could take place.

It might be feasible for ASEAN banks to create an interbank market among themselves. It was pointed out in section II that some ASEAN banks are net lenders in the international interbank market, while others are net borrowers. Thus, the potential for developing this market already exists.

Beyond the ASEAN region, it might be necessary for ASEAN banks to participate in some of the activities of established international

banks. The country funds that have been recently created for ASEAN countries could have been one of such opportunities. All of these funds are being managed by international banks with practically no participation from ASEAN banks. However, some of the activities, such as formulation of proposals for client firms, could have been easily done by ASEAN banks.

Finally, multilateral liberalization of trade in banking services will hopefully give more opportunities for ASEAN banks to increase their physical presence in other countries, especially those that have been their important trading partners. There are strong indications that such liberalization under a multilateral framework agreement will be more beneficial to ASEAN countries as well as other developing countries than a bilateral agreement.

Box 1

FINANCIAL SERVICES IN THE URUGUAY ROUND

The course of negotiations on financial services in the Uruguay Round has been determined by a number of factors peculiar to the sector, including its role as a tool of monetary and development policy and the jealously guarded responsibilities of Finance and Treasury Departments and Central Banks. As in some other service sectors, the negotiations are also strongly influenced by "Europe 1992", [a] in particular, by the "Second Banking Coordination Directive". This directive specifies the conditions under which a credit institution authorized in one member State (including credit institutions owned or controlled in non-member States) may offer a full range of financial services directly to customers in other member States without further authorization - i.e. the "single passport", a right enjoyed by existing foreign-controlled banks established in any of the 12 member States. This regime, described as one of the most open banking markets in the world, contrasts with that of the other major financial powers. In the United States, there is a sharp division under the Glass-Steagall Act between banking and dealing in securities, and banks may be authorized and regulated by individual states. In Japan, the banking and securities markets have traditionally been separated and access to the market has been based on reciprocity.

Reciprocity considerations shaped the debate leading to the formulation of the Second Banking Directive (which will come into effect in 1993), in that there was concern that foreign banks should not be given access to the "single passport" if their home countries did not provide equivalent treatment to EC banks. Although the original more stringent reciprocity proposals have been somewhat diluted, the Second Banking Directive contains provision for retaliation, against countries which do not provide "national treatment offering the same competitive opportunities" and "effective market access" for EC credit institutions. In addition, there are provisions for bilateral negotiations, in parallel with the Uruguay Round, aimed at securing "competitive opportunities comparable to those offered by the EC to foreign institutions". This has prompted the EC to submit a proposal for a "sectoral annotation" to the multilateral framework on trade in services being negotiated in the Uruguay Round, which would, in effect, oblige signatories to provide such comparable competitive opportunities by establishing an extremely liberal international regime for financial services.

The United States has come up with a counter-proposal which also envisages a liberal regime but differs from the EC proposal in important aspects. For example, the United States appears to favour a separate, self-contained agreement which would be applied conditionally, only the signatories to the sectoral agreement and not to all the parties to the multilateral framework. [b]

From the point of view of the interests of the Asia and Pacific region, the negotiations on financial services are notable in that this is the one area of the Uruguay Round where developing countries of the Region have put forward a joint, independent proposal. The Member States of the South-East Asia Central Banks and Monetary Authorities (Indonesia, Malaysia, Thailand, Nepal, Sri Lanka, the Republic of Korea, the Philippines, Singapore and Myanmar) have outlined their position as follows:

(i) Financial services should be included in the coverage of the multilateral framework for trade in services (MFTS). As such, there should not be a separate agreement on financial services.

(ii) The sectoral annotations on financial services should form an integral legal part of the MFTS. The sectoral annotations should not impose more onerous obligations on the financial services sector to liberalize compared with the other services sectors.

Box 1 (Continued)

FINANCIAL SERVICES IN THE URUGUAY ROUND

(iii) The process of financial liberalization must take cognizance of the over-riding importance of prudential consideration, monetary policies and national development objectives. In developing countries like SEACEN members, financial services play a pivotal role in economic development. Hence, liberalization must ensure that developments in the financial sector do not adversely affect the effectiveness of national institutions and the overall general well-being of the economy. It should also allow flexibility to nations in the design and implementation of banking and credit policies which are normal functions of a central bank or monetary authority.

(iv) Financial liberalization would only be mutually meaningful and beneficial to the financial institutions of the host and foreign countries if they are equally well established. However, most of the financial institutions of SEACEN countries do not have the benefit of a long banking tradition which dates back to history. Therefore, the liberalization of financial services in the SEACEN countries should be gradual, yet progressive, taking full cognizance of the level of development of their financial sectors vis-à-vis those of the more developed countries.

(v) Market access should not imply automatic national treatment given the different levels of efficiency and expertise between foreign and local financial institutions. Once established, foreign financial institutions have the added advantage of an effective global network and special traditional relationships. Some flexibility in the national treatment rule is necessary to reduce such inequalities to level the competitive field for all financial institutions.

(vi) Given the different stages of development in financial services among countries, commitments to the MFTS for financial services should be adopted on a positive list approach.

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a See R. de C. Grey, "1992, Service Sectors and the Uruguay Round", in *Trade in Services: Sectoral Issues* (United Nations Publication, UNCTAD/ITP/26), as well as "1992, Financial Services and the Uruguay Round", UNCTAD, 1990 (forthcoming).

b The EC and United States proposals have been discussed in earlier UNCTAD publications, particularly by Andrew Cornford and R. de C. Grey, *op. cit.*, as well as by Mario Lamberte in this volume.

Box 2

MONETARY POLICY AND MARKET ACCESS

It is important to make a clear distinction between "market access", which covers the right of entry to particular banking sub-markets, and "national treatment", which concerns the treatment received from the authorities by a supplier of banking services after the granting of such access. Control over market access is the policy instrument perhaps most crucial to enabling governments in developing countries to choose the banking regimes which they believe to be most appropriate to their particular circumstances and needs. . . . Banking consists of several sub-markets, and the access granted to foreign banks generally applies only to certain of them. Thus control over such access makes it possible for governments to pursue policy objectives towards the different constituent parts of a country's banking system.

These policy objectives may concern various subjects . . . Particularly important here are the objectives which may be pursued through infant-industry policies for financial sectors and other policies that can be expected to play a role in eventually increasing the participation of developing countries in international trade in banking services. Thus, for example, control over market access can serve as an instrument for the achievement of the transfer of banking skills. Furthermore, such control can be used to influence the level and character of competition in banking. By this means it should be possible to avoid certain adverse effects of such competition, while employing the entry of foreign banks as a stimulus to increasing efficiency among indigenous ones. In particular, control over market access enables governments to restrict activities likely to be associated with financial instability, and to protect indigenous banks from premature exposure to unfair pricing practices. Moreover, control over market access may enable governments to reconcile the objectives of liberalizing regimes for foreign banks, on the one hand, and of maintaining desired levels of autonomy in the conduct of monetary policy, on the other.

Andrew J. Cornford, "Notes on a Multilateral Framework on Trade in Banking Services", in UNCTAD, Uruguay Round: Further Papers on Selected Issues *(United Nations Publication, UNCTAD/ITP/42), pp. 186-7.*

Table 1

BANKING DENSITY IN ASEAN COUNTRIES, 1988

	Indonesia	*Malaysia*	*Philippines*	*Singapore*	*Thailand*
Population (in millions)	175.22	16.90	58.80	2.60	54.55
No. of banking offices	7,423	1,548	3,562	729	2,655
Banking density	23,605	10,917	16,507	3,566	20,546

Source: Asian Development Bank, *Asian Development Outlook 1990* (Manila, ADB, 1990); Philip. Erquiaga, "Improving Domestic Resource Mobilization through Financial Development - Indonesia", *ADB Economic Staff Paper*, No. 40; Lin See-Yan *et.al.*, "Money Market in Malaysia", unpublished, 1990; Central Bank of the Philippines, *1988 Fact Book: Philippine Financial System* (Manila, Central Bank of the Philippines, 1988); Amina Tyabji, "Financial Reform in ASEAN", unpublished, 1989; Bank of Thailand, "Financial Institutions and Market in Thailand", December, 1989.

Note: This includes only offices of the banking system. For Indonesia, the number of banking offices is as of March 1988.

Table 2

FINANCIAL INSTITUTIONS IN INDONESIA, SEPTEMBER 1989

Type of financial institution	*Number of Head offices*	*Total assets (Rp.bil.)*	*Percentage*
Deposit money banks (DMBs)	141	85,740	86.3
State banks	5	51,450	51.8
Joint ventures [a]	12	-	-
Foreign bank branches	10	4,626	4.7
Development banks	29	6,384	6.4
BAPINDO	1	3,886	3.9
Regional development banks	27	2,498	2.5
Private	1	-	-
Private banks	85	23,469	23.6
Non-Foreign Exchange	64	7,510	7.6
Foreign Exchange	21	15,959	16.1
Rural financial institutions	7,713	579	0.6
Existing before PAKTO	7,236	55	0.1
Established after PAKTO	477	524	0.5
Savings banks:			
State Savings Bank (BTN)	1	2,531	2.5
Private savings banks	4	-	-
Pawnshops (State-owned) [b]	1	152	0.2
State Securities & Investment Fund Co. (DANAREKSA)	1	298	0.3
Non-Bank financial institutions	13	3,564	3.6
Development finance institutions	3	837	0.8
Investment finance institutions	9	2,413	2.4
Housing finance (Papan Sejahtera)	1	314	0.3
Insurance	130	3,906	3.9
Life	30	799	0.8
Loss	77	844	0.9
Social insurance [c]	5	1,930	1.9
Reinsurers	4	333	0.3
Adjusters	14	-	-
Pension funds [d]	130	1,329	1.3
TASPEN	1	1,105	1.1
Others	129	224	0.2
Securities companies	7	-	-
Brokers/dealers	129	-	-
Non-Deposit financial institutions	154	-	-
Leasing companies	101	1,195	1.2
Factoring	14	-	-
Venture capital	7	-	-
Credit card	11	-	-
Consumer finance	21	-	-
Total	8,424	99,294	100.0

Source: David Cole, and Betty F. Slade, "Development of Money Markets in Indonesia", unpublished, 1990.

a These banks are joint-ventures between Indonesian and foreign banks.

b There is one pawnshop office with 498 branch offices

c Includes ASABRI, the military employees social insurance fund.

d Excludes unknown number of pension funds that are not registered with the Ministry of Finance.

Table 3

THE FINANCIAL SYSTEM IN MALAYSIA, 1988

Type of institution	*Number of Head offices*	*Assets (M$ mil.)*	*Percentage*
I. Banking institutions			
Commercial banks	38	93,021	31.87
Domestic	22	69,500	23.81
Foreign	16	23,521	8.06
Islamic Bank	1	1,429	0.49
Finance	47	24,283	8.32
Merchant banks	12	7,026	2.41
Discount houses	7	2,211	0.76
Total	143	220,991	75.71
II. Non-Bank financial intermediaries			
Development finance institutions	7	3,500	1.20
Savings institutions	14	2,487	0.85
Provident pension funds [a]	10	47,490	16.27
Insurance companies	105	7,011	2.40
Other financial intermediaries [a]	7	10,401	3.56
Total	143	70,889	24.29
Grand Total	286	291,880	100.00

Source: Lin, See-Yan, *et al*., "Regional Research Project: Study of Money Markets in Asia", unpublished, 1990.
a Only 6 large ones are included.

Table 4

THE PHILIPPINE FINANCIAL SYSTEM AS OF 31 DECEMBER 1988

	Number of head offices	*Amount (Billion P)*	*Percentage*
Banking system	982	360.1	72.0
Commercial banks	29	299.3	59.8
Private	24	224.6	44.9
Government	1	38.8	7.8
Foreign	4	35.9	7.2
Thrift banks	110	24.9	5.0
Savings and mortgage banks	8	14.2	2.8
Private development banks	41	6.7	1.3
Stock savings and loan associations	61	4.0	0.8
Rural banks	840	10.7	2.1
Specialized government banks	3	25.2	5.0
Non-bank financial intermediaries	2,766	140.2	28.0
Insurance companies	135	98.3	19.6
Government	4	68.6	13.7
Private	131	29.7	5.9
Investment institutions	233	21.4	4.3
Financing companies	143	7.4	1.5
Investment companies	75	5.6	1.1
Investment houses	15	8.4	1.7
Trust operations (fund managers)	12	1.8	0.4
Other financial intermediaries	2,386	18.7	3.7
Total	3,758	500.3	100.0

Source: *Philippine Financial Fact Book, 1988*; Insurance Commission (for data on insurance companies in 1988); Government Corporate Monitoring and Co-ordinating Committee for assets of SSS and GSIS in 1988.

Table 5

AUTHORIZED ACTIVITIES OF VARIOUS BANK CATEGORIES IN THE PHILIPPINES BASED ON THE AMENDED BANKING LAWS

Authorized Activities	Expanded Commercial banks (Unibank)	Commercial banks (KBs) Domestic	Commercial banks (KBs) Foreign	Thrift banks: Savings and mortgage banks	Thrift banks: Private and dev. banks	Thrift banks: Savings and loan Association	Rural banks
A. Commercial banking services							
1. Accept deposits	1	1	1	1	1	1	1
2. Issue LCs & accept drafts	1	1	1[a]	1[a]	1[a]	1	xx
3. Discounting of promissory notes and commercial papers	1	1	1	1	1	1	1
4. Foreign exchange transactions	1	1	1	x	x	x	xx
5. Lend money against security	1	1	1	1	1	1	1
B. Nation-wide branching operations	1	1	1	1	1	1	1
C. Equity investments in allied undertakings	x	x	x	x	x	x	x
D. Equity investments in non-allied undertakings	1	xx	xx	xx	xx	xx	xx
E. Trust operation	x	x	x	x	x	x	x
F. Issue real estate and chattel mortgage; bonds; buy and sell these for its own account, accept/receive in payment or as amortization of loan	1	1	1	1	1	1	1
G. Direct borrowing with Central Bank	1	1	1	1	1	1	1

Table 5 (Continued)

AUTHORIZED ACTIVITIES OF VARIOUS BANK CATEGORIES IN THE PHILIPPINES BASED ON THE AMENDED BANKING LAWS

Authorized Activities	Expanded Commercial banks (Unibank)	Commercial banks (KBs)		Thrift banks			Rural banks
		Domestic	Foreign	Savings mortgage banks	Private and dev. banks	Savings and loan Association	
H. Activities of an investment house							
1. Securities underwriting	1	xx	xx	xx	xx	xx	xx
2. Syndication activities	1	1	1	1	1	1	1
3. Business development and project implementation	1	1	1	1	1	1	1
4. Financial consultancy and investment	1	1	1	1	1	1	1
5. Mergers and consolidation	1	1	1	1	1	1	1
6. Research and studies	1	1	1	1	1	1	1
7. Lease real and/or personal properties	xx	xx	xx	xx	xx	xx	xx
I. Money market operation	1[b]	1[b]	1[b]	xx[b]	xx[b]	xx[b]	xx[b]

Source: Mario B. Lamberte, "The Financial System of the Philippines: Operations and Problems", unpublished, July 1990.

Note: 1 = Authorized activities; x = Authorized but subjected to Monetary Board approval; xx = Not authorized/prohibited.

a Limited only to domestic LCs and drafts.

b The lending side may be done by all banks without prior CB approval. The borrowing side (quasi-banking) may be exercised only with prior CB approval for all banks.

Table 6

PHILIPPINE OFFSHORE BANKING SYSTEM, STATEMENT OF ASSETS AND LIABILITIES, SEPTEMBER 1989

Items	*(Million dollars)*
Assets	
Notes and coins in hand	-
Due from banks	1,506
Outside the philippines	359
In the Philippines	1,147
Loans and discounts to customers	
Other than banks	1,096
Non-residents	115
Residents	981
Public sector	481
Private sector	500
Bills discounted/purchased	1
Non-residents	-
Residents	8
Investment in bonds and other securities	28
Non-residents	20
Residents8	
All other assets	86
Interest receivable	40
Non-residents	8
Residents	32
Other assets in the Philippines	45
Other assets outside the Philippines	1
Total assets	2,717
Less allowance for probable losses	20
Total assets after allowance for losses	2,697
Liabilities	
Deposit of non-residents other than banks	40
Due to banks	2,554
Outside the Philippines	2,205
In the Philippines	349
Other liabilities	103
Interest payable	37
Non-residents	33
Residents	4
In the Philippines	31
Outside the Philippines	35
Total liabilities	2,697

Source: Foreign Exchange Regulations Department, Central Bank of the Philippines.

Table 7

MONEY MARKET INSTITUTIONS IN SINGAPORE, 1988

	Number of Head Offices
Commercial Banks	
Local full license banks	13
Foreign	121
Full license banks	22
Restricted banks	14
Offshore banks	85
Asian Currency Units (ACUs)	187
Merchant banks	63
Finance companies	31
National Saving Bank (POSB)	1
Discount Houses	-
International Money Brokers	8

Source: M. Ariff, B. Kapur, and A. Tyabji, "Money Market Study: Singapore", unpublished, 1990.

Table 8

ASSETS OF MONEY MARKET INSTITUTIONS IN SINGAPORE, 1988

Bank type	*S$ million*
Commercial banks	
Domestic operations	96,441
Domestic and offshore	586,215
Merchant banks	
Domestic operations [a]	8,274
Domestic and offshore	36,942
Finance companies	8,479
Discount houses [b]	2,458
National Savings Bank [c]	12,262
Total	646,338

Source: M. Ariff, B. Kapur, and A. Tyabji, "Money Market Study: Singapore", unpublished, 1990.

a Figures do not reflect corporate financial advisory services, underwriting and operations in the gold market.

b Discount houses were discontinued in 1986.

c Total depositors' balances.

Table 9

SINGAPORE COMMERCIAL BANKS: ASSETS AND LIABILITIES, 1988
(In S$ million)

Items	*Excluding ACUs* Amount	*Excluding ACUs* Percentage	*Including ACUs* Amount	*Including ACUs* Percentage
Assets				
Cash on hand	568	0.6	590	0.1
Balances with MAS	2,371	2.5	2,371	0.4
Amount due from banks	38,148	39.6	380,953	65.0
Money at call with discount houses	-	-	-	-
S$ NCDS held	146	0.2	2,660	0.5
Investments in securities and equities	9,053	9.4	25,616	4.4
Loans and advances (including bills)	41,849	43.4	160,293	27.3
Other assets	4,307	4.5	13,731	2.3
Total assets	96,441	100.0	586,215	100.0
Liabilities				
Capital and reserves	6,760	7.0	8,058	1.4
Deposits of non-bank customers [a]	42,475	44.0	125,469	21.4
S$ NCDs issued	993	1.0	5,106	0.9
Amount due to banks	39,328	40.8	427,544	72.9
Other liabilities	6,886	7.1	20,037	3.4
Total liabilities	96,441	100.0	586,215	100.0

Source: M. Ariff, B. Kapur, and A. Tyabji, "Money Markets Study: Singapore", unpublished, 1990.

a Singapore dollar negotiable certificates of deposits (S$ NCDs) were first issued by banks in May 1975.

Table 10

FINANCIAL SYSTEM IN THAILAND, 1988

Type of financial institution	*Number of head offices*	*(million Bahts)*	*Percentage*
I. Banking system			
Commercial banks	30	1,596,780	76.68
Domestic	16	1,513,795	72.70
Foreign	14	82,985	3.99
Government Savings Bank	1	124,273	5.97
Government Housing Bank	1	19,524	0.94
Bank for Agriculture and Agricultural Co-operatives	1	37,326	1.79
Total	63	1,777,903	85.38
II. Non-bank financial intermediaries			
Finance and securities companies	94	195,687	9.40
Credit Foncier companies	19	3,918	0.19
Agricultural co-operatives	1,251	13,959	0.67
Savings co-operatives	785	30,898	1.48
Life insurance companies	12	29,257	1.41
Pawnshops	338	6,505	0.31
Industrial Finance Corporation of Thailand	1	24,105	1.16
Small Industries Finance Office	1	78	0.00
Total	2,501	304,407	14.62

Source: Bank of Thailand, "Financial Institutions and Market in Thailand", unpublished, December 1989.

Table 11

BRIEF PROFILE OF ACTIVITIES OF SIX TYPES OF FINANCIAL INSTITUTIONS IN THAILAND AS OF 1984

Institutions	*Activity*	*Supervising Institution*
1. (1.1) Commercial banks	(1) Mobilize funds by taking deposits from the public (2) Lending in the form of loan, overdraft and bill discounting (3) Investing in securities	Bank of Thailand
(1.2) Government Savings Bank	(1) Mobilize funds by taking deposits from the public (2) Investing in government securities (3) Lending to the public	Bank of Thailand
(1.3) Government Housing Bank	(1) Mobilize funds by taking deposits from the public (2) Lending to the public for housing purposes	Ministry of Finance
(1.4) Bank for Agriculture and Agricultural Co-operatives (BAAC)	(1 Taking deposits from the public (2) Lending to farmers and agricultural co-operatives	Ministry of Finance
2. (2.1) Finance and Securities Companies	(1) Issuing promissory notes (2) Purchasing promissory notes (3) Investing in securities	Bank of Thailand
(2.2) Credit Foncier Co.	(1) Mobilize medium-term funds (not less than 3 years) from the public by issuing promissory notes at a minimum amount of Baht 1,000 per note (2) Lending for housing purposes	Ministry of Finance
3. (3.1) Agricultural Co-operatives	(1) Main sources of funds are borrowings from BAAC and members' subscriptions to capital account (2) Lending directly to their members	Ministry of Agriculture and Agricultural Co-operatives
(3.2) Savings Co-operatives	(1) Main sources of funds are paid-up share capital and members' savings (2) Lending short-term and long-term funds to members	Ministry of Agriculture and Agricultural Cooperatives

Table 11 (continued)

BRIEF PROFILE OF ACTIVITIES OF SIX TYPES OF FINANCIAL INSTITUTIONS IN THAILAND AS OF 1984

Institutions	*Activity*	*Supervising Institution*
4. Life insurance companies	(1) Selling life insurance policies to the public (2) Lending and investing in securities	Ministry of Commerce
5. Pawnshops	(1) Main sources of funds are their own savings and borrowings from financial institutions (2) Lending money against a variety of articles, jewelry, gold, machine, electrical appliances, etc.	Ministry of Interior
6. (6.1) Industrial Finance Corporation of Thailand (IFCT)	(1) Borrowing long-term funds from both domestic and foreign sources (2) Extending medium- and long-term credits to industries	Ministry of Finance
(6.2) Small Industries Finance Office	(1) Receiving funds appropriated from the government budget and then depositing them with the Krung Thai Bank. Krung Thai Bank also provides matching amounts to SIFO's account - at the ratio of 3 to 1 - for the purpose of lending to small industries	Ministry of Finance and Ministry of Industry

Source: Thailand Development Research Institute (TDRI), "1986 Year-End Conference on Financial Resources Management", unpublished, December 1986.

Table 12

ESTABLISHMENT TRADE IN FINANCIAL SERVICES IN COUNTRIES OF THE PACIFIC REGION

Country	*Total number of branches and subsidiaries of ASEAN banks in other countries of the Pacific region*	*Total number of branches and subsidiaries of banks of other countries in the Pacific region established in ASEAN countries*
Indonesia	14	41
Malaysia	15	31
Philippines	33	33
Singapore	52	113
Thailand	22	30

Source: Kazuma Iwata, 'Liberalization of Trade in Financial Services', Castle, Leslie and Findlay (eds.), *Pacific Trade in Services* (Sydney, Allen and Unwin, Inc., 1988).

Table 13

NUMBER OF OVERSEAS BRANCHES OF TOP TEN BANKS IN ASEAN COUNTRIES

Bank name	*Mid-70s*	*1983*	*Change*
Indonesia			
Bank Negara Indonesia	3	3	0
Total	3	3	0
Malaysia			
Bank Bumiputra (M) Bhd	na	6	+6
Malayan Banking Bhd	26	26	0
United Malayan Banking Corp.	9	9	0
Total	35	41	+6
Philippines			
Philippine National Bank	3 [a]	4	+1
Allied Banking Corporation	na	3	+3
Total	3	7	+4
Singapore			
Development Bank of Singapore	na	4	+4
United Overseas Bank	4	32 [b]	+28
Oversea-Chinese Banking Corp.	31	31	0
Overseas Union Bank Limited	19	18	-1
Chung Khiaw Bank	18	18	0
Lee Wah Bank	9	9	0
Total	81	112	+31
Thailand			
Bangkok Bank	15	12	-3
Krung Thai Bank	-	1	+1
Thai Farmers Bank	1	3	+2
Siam CommercialBank	-	2	+2
Total	16	18	+2

Source: John Newson, 'The Internationalization of Banking', Agustine Tan and Basant Kapur (eds.), *Pacific Growth and Financial Interdependence* (Massachusettes, Allen and Unwin, Inc., 1986).

Note: Banks are ranked by total assets in the year to 31 December 1982.

a Including agencies.

b Two subsidiaries.

Table 14

ASEAN: INTRA-ASEAN OPERATING COMMERCIAL BANKS, 1981

Parent Country	*Bank*	*Host country*
Indonesia	(1) Bank Negara Indonesia	(1) Singapore
Malaysia	(1) Malayan Banking Berhad	(1) Brunei (2) Singapore
	(2) United Malayan Banking Corp.	(1) Brunei (2) Thailand
	(3) Ban Hin Lee Bank	(1) Singapore
	(4) Malayan United Bank	(1) Singapore
	(5) Bank Bumiputra Malaysia Berhad	(1) Singapore (off-shore)
Philippines	(1) Philippine National Bank	(1) Singapore (off-shore)
Singapore	(1) Overseas Union Bank	(1) Brunei (2) Malaysia
	(2) Chung Kiaw Bank	(1) Malaysia
	(3) Lee Wah Bank	(1) Malaysia
	(4) Overseas Chinese Banking Corp.	(1) Malaysia
	(5) United Overseas Bank	(1) Malaysia
	(6) Four Seasons Communication Bank	(1) Thailand
	(7) International Bank of Singapore	(1) Philippines (off-shore)
Thailand	(1) Bangkok Bank	(1) Indonesia (2) Malaysia (3) Singapore

Source: D.M Sutalaksana, "Commercial Banking Links in ASEAN", Staff Paper No. 15, SEACEN Research and Training Centre, 1986.

TRADE IN MEDIA SERVICES: ASIA AND THE PACIFIC REGION

*Malati Tambay Vaidya**

INTRODUCTION

This paper attempts to assess the potential effects of trade liberalization in the media sector, with a view to increasing the participation of Asian and Pacific media services in the international market. For the purpose of this paper, the term 'media' includes films and television. The emphasis is on the comparative study of international trade in media services with respect to six selected countries and territories - namely, Australia, India, Japan, Republic of Korea, Hong Kong and Singapore. The paper covers the following issues:

- Structure of market and competition in the media service industries, as well as the link with trade in goods in the countries;
- Factors relevant for their relatively successful export of media services;
- Problems which the countries face in expanding the export of media services, particularly in relation to the control of distribution channels by major producers;
- Impact of technological advance on the international trade in media services;
- Possibilities for Asian countries in increasing foreign exchange earnings from the media service industry, including through the Uruguay Round negotiations on trade in services.

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The concept of film making was introduced to the world when in 1896, Lumière Brothers from France displayed their movie camera in France and in some other countries including India. Movie making on a regular basis started in some countries in the first quarter of the present century. The era of silent film was followed by that of talkies and later that of colour film. The movie industry has, by now, completed more than 75 years of its existence in a number of countries.

The film industry has, however, grown steadily since its inception and appears to have reached a plateau as far as production of long films is concerned. There are about 65 film-producing countries in the world, and their total output is estimated to be ranging between 4,000-4,500 films per year. Asia has always been dominant in this field, its share of the world's film production ranging from 24.3 to 33 per cent during the past decade. North America comes third with its percentage share ranging from 5 to 15.1 during the same period. Countries from Oceania and Africa did not contribute practically until 1975, and even after that their production has been less than 1.5 per cent.

Europe, including USSR, enjoys a dominant position in terms of fixed cinemas, seating capacity and attendance. However, the number of cinemas has declined in Europe over the past decade. On the other hand, in Asia, the figures have gone up, although seating capacity has not kept pace with the increase in population. The attendance figures have been sliding down in Europe, North America, Latin America and Oceania, while more and more people have been going to cinemas in Asia and Africa.

Television entered the field of media services after 1950, and the number of television transmitters/receivers has been increasing steadily since then. Europe, including USSR, occupies the most prominent position on the television front, followed by Asia, North America and Latin America - in that order. North America is second to Europe in the number of television receivers, followed by Asia and Latin America. However, North America has the maximum number of television receivers per 1000 inhabitants, followed by Europe, Oceania, Latin America and Asia. Asia does not thus have adequate number of receivers corresponding to the number of transmitters and to its population. In some of the countries like India, TV receivers are used for

community viewing, providing better access for the population than is reflected by number of receivers.

Films have been shown mostly in cinemas for several decades. However, with the advent of television, films began to be telecast and people had the opportunity to view them at home. Earlier, films were handled between three constituents - the producer, the distributor and the exhibitor within a country, and when they were to be shown in a country other than the country of origin, the exporter/importer came into the picture. This has traditionally been accepted as the general pattern.

Though the international trade patterns for film and television programmes are not exactly identical, it is justifiable to consider them together for two reasons - firstly, production facilities and ownership of the two media, particularly in the major producing countries, share several common features. Secondly, film and television programmes are similarly affected by many of the concepts and principles being proposed as elements of a multilateral framework for trade in services, as well as those covering intellectual property.

I. MEDIA SERVICES WITHIN THE SERVICE SECTOR

Trade regulation necessarily rests on assumptions about the nature of the product to be traded and about the ways in which it is produced and distributed. Film and television programmes are particularly difficult subjects within the negotiating context because, although they can be defined as tradable products, they are also part of a broader sphere of audio-visual activities, many of which have non-commercial (scientific, cultural and educational) objectives. Many countries subsidize and regulate national media under the belief that radio and television broadcasting as well as film have specific purpose, in addition to that of commercial entertainment, such as cultural and individual expression and social communication.

The elaboration of general concepts and principles affecting trade in services is difficult, given that service industries differ considerably from one another. Even apart from disagreements as to whether media can be reduced to a tradable product, there are differences in the way

in which films and television programmes are produced and distributed that distinguish them from other services such as insurance or banking. These differences in purpose, production and distribution need to be examined in detail before any evaluation of the development implications of altering trade regulations can be made.

Film and television programming are distinguishable in purely economic terms from other services in several respects. Firstly, the production of a film or television programme resembles manufacturing insofar as there is an actual physical product, composed of labour and capital-intensive inputs. Hence, in comparison with services such as tourism, construction and, particularly, professional services, where employment occurs and value is added at the final destination of the service, films and television programmes are finished products which are merely distributed at their final destination. The distancing of production and distribution in these industries virtually eliminates possibilities for technology transfer or highly skilled employment at the point of distribution. The production of media products is organized in such a way that almost all the labour inputs and definitely all the skilled labour inputs occur in centralized locations far removed from the distribution point.[1]

Secondly, all the costs in making the product are incurred in turning out the first copy of the film or television programme. Additional copies can be produced relatively inexpensively. So, profitability in this sector depends on the timing and strategic control of release of the film or programme, a process that has become more complicated as the number of different types of potential distribution outlets has multiplied world-wide. This constraint on potential profit intensifies the need to control distribution very tightly through, for example, the ownership of distribution networks.

Films and television programmes are not standard commodities like steel or soap where the different products on sale are generally similar and with the same specifications. Further, the fact that the film or television programme has been seen by one person in the same

1 Susan Christopherson and Stephen Ball, "Media Services: Considerations Relevant to Multilateral Trade Negotiations", in UNCTAD, *Trade in Services: Sectoral Issues* (United Nations Publication, UNCTAD/ITP/26), pp. 249-308.

country or abroad does not reduce what is available for consumption by others. For films and television programmes, the value of the product to consumers is determined almost entirely by such public good elements as the appeal of the story presented, the quality of scripts/screenplay, the perspective of the director and the competence of camera crews and other technical personnel. Therefore, the price at which the film or programme is sold in one country is not necessarily related to the sales and earnings in another country. The product we are dealing with is thus unique, and the prices paid for it are affected by a large number of considerations that vary from country to country, the important ones amongst them being population, number of persons who understand the language in which the product has been made, per capita income, structure of domestic film exhibition and television industries, and government policies of the producing countries. The cost of production also is relevant here.

In view of this, three different types of data need to be used in order to describe film trade and its effects. These three types correspond to (a) numbers of films crossing national boundaries, (b) impact of imported films on domestic film markets and audiences, and (c) financial flows associated with the trade in films. In turn, three types of data that correspond to these three aspects of trade - i.e. data based on counts of films produced and imported on a country-by-country basis, data on the audiences and box-office revenues generated by foreign and domestic films for a variety of countries, and data on financial payments - are vital.

A. Films

The annual tallies of production and import statistics compiled by UNESCO are by far the most comprehensive source of data on the numbers of films produced and traded world-wide. These statistics cover a majority of United Nations member countries. The figures reported in table 1 are based on UNESCO statistics. Most countries produce relatively few films and import most of the films viewed by its citizens. Not surprisingly, domestically produced films generally account for a larger proportion of films shown in the major films producing nations.

The negative relationship between domestic film production and domestically produced films as a fraction of total films is quite evident from the UNESCO statistics. Slightly more than half of the 66 countries represented in it produced 20 or fewer films annually, about 70 per cent produced 40 or fewer. More than three quarters of the countries produced 60 films or fewer. Just three countries produced more than 150 films. Domestic production accounted for over 30 per cent of total films shown in all three countries and for more than 50 per cent of the total in two of them.

On the import front, all the 66 countries imported more than 20 per cent of the total number of films. 71 per cent of the countries depended on foreign films to the extent of 80 per cent of their supply. One country producing more than 300 films, i.e. India, imported only around 20 per cent of foreign films every year.

It can safely be surmised from table 1 that the few countries producing films in large numbers would be the major suppliers of films to the majority of countries that import most of their films. From the data collected, nine countries are identified and listed in table 1 as a major film-exporting countries. Four indices have been applied in this table and on all four of them, United States tops the list, being the largest supplier of imported films in 49 of the 85 countries in the sample. The Soviet Union as the principal supplier for 13 countries, and India as the principal supplier for nine countries, are a distant second and third. It is interesting to note that from Asia, three countries - India, Hong Kong and Japan - figure in the list. Regional trading relationships and linguistic, cultural and political ties, which are not reflected in this table, are evident in the UNESCO statistics. Mexico is an important source of imported films in Latin America. While French films are imported by countries throughout the world, they are particularly popular in countries related to France through linguistic and historical ties. Films from Hong Kong are imported in all regions of the world, but they generally make up larger shares of imports in South-East Asian countries. Importation of Indian films is concentrated in Africa, South-East Asia, and the Arabic-speaking countries of the Gulf and Middle East, due to the presence of ethnic population of Indian origin or familiarity of these countries' population with Indian films, to historical association and to cultural affinities. Table 1 also

shows that films produced in the larger European countries are exported throughout the world. They make up a significantly larger share of all the films within Western Europe.

B. Television

The number of television receivers in the world has gone up by nearly four times between 1965-1987, while the number of transmitters has gone up ten times. The demand for more and more programmes has thus been continuously on the increase. United States is by far the largest supplier of imported television programmes in most areas of the world. The other major suppliers besides United States are United Kingdom, France, Federal Republic of Germany and Japan. Imports accounted for only a fraction of the programmes shown on American television. By contrast, imported programmes accounted for approximately one-third or more of total programming time in other countries. The existence of distinct regional areas with their own important suppliers, in addition to the countries identified as major global producers, is also clear. Important regional suppliers include Brazil and Mexico in Latin America, Egypt in the Arab world, Hong Kong in South-East Asia and the Soviet Union in Eastern Europe. In Western Europe, such regional television exchanges as Eurovision contribute to intraregional programme flows. In general, the Eastern European countries have until now bought programmes from and sold programmes to one another.

C. Language angle

The film or television programme can be screened with subtitles or in dubbed version in the language of the country where it is shown, in order to enable viewers of that country to enjoy the film. subtitling or dubbing skills are well-developed, and the necessary machinery is available in the market. As viewers prefer to view a film or television programme in their own language, there is a clear link between language and marketability. Table 2 gives a clear picture of the language angle. Perusal of table 2 along with table 1 shows that it is not just the number of people who speak a particular language that matters for marketability of products in that language. Whether this population lives in the same

country or in different countries is also important. For exports, the relevant factor concerns how many people speaking a language stay abroad and whether they stay together in large groups in specified countries or are spread all over. Thus, though Mandarin, Hindi and Urdu are spoken by a very large number of people, the highest exports are of English language products. This is not only because English is the first language in United Kingdom, United States, Australia, New Zealand and a major part of Canada, but also because English is widely understood in all the countries which constituted the British Empire for a considerable period of history. Linguistic and cultural links are also important for the export of films in the French, Spanish and Arabic languages.

II. MARCH OF TECHNOLOGY

A. Video

We noted earlier that the advent of television introduced a major change in the location of film projection, enabling viewers to watch films at home. Television also led to production of television films and special programmes including television serials, contributing to a wider variety of audio-visual material available to viewers all over the world. Video technology made its appearance for the first time when Ampex Company demonstrated and marketed video equipment in 1956. Philips introduced the first colour cassette recorder in 1974, but it was not until 1978 that the first reliable colour systems came on the market - Sony's Beta and JVC's VHS systems, which have come to dominate world markets.

Video technology has become omnipresent because of its versatility. Television broadcasting leans heavily on video everywhere because of its immediacy and its usefulness in activities as diverse as news gathering, advertising, education and training, scientific and medical examination and experimentation, and recreation in the form of the "home movie". Introduction of 'camcorders' or camera with inbuilt video recorders brought about the production of special programmes or recording of personal or family events within the reach of individuals. General interest tapes about gardening, cooking, motor repairs, 'keep

fit', management, etc. began appearing in the markets, catering to the requirements of different interest groups, including the ethnic groups in society.

B. Satellites

After the International Telecommunications Satellite Organisation (INTELSAT) achieved "global" signal coverage with the successful operation of satellites over the Atlantic, Pacific and Indian Oceans in 1969, the importance of satellite distribution of television programmes has increased dramatically. The INTELSAT consortium offers services to 109 member nations around the world. In addition, non-member nations can purchase satellite time, bringing the total number countries with access to INTELSAT to 170. Each nation maintains one or more earth stations that allow access to all other participating nations via satellite connection.

Several groups of nations joined thereafter to initiate regional satellite associations. ARAB-SAT, a consortium of twenty-two Middle East and North African countries, proposed a pan-Arab television broadcast service. Five Nordic countries came out with a proposal to have NORDSAT as the satellite for their region. In Europe, the European Space Agency (ESA) launched the satellite ECS-1 in 1983, with nine transpoders allocated among the Federal Republic of Germany, United Kingdom, Belgium, France, Italy, the Netherlands, Norway and Sweden. Many other satellites followed. There are currently more than 133 communication satellites in geo-stationary orbit. They are utilized to transmit voice, data and video images internationally as well as to send television programmes around the world by using several satellites. These satellites signal in several ways:

- Satellite to broadcaster,
- Satellite to broadcaster to cable system,
- Satellite to cable system,
- Satellite to pay-TV (subscriber-supported television) or SMATV (Satellite Master Antennae Television) systems,

- Satellite to theatre, and
- Satellite to home.

Satellite can deliver signals directly to the subscriber's home if the home is equipped with a home-reception antenna. For such direct broadcasting satellites (DBS) direct reception antennae are available, but they are very expensive at present. If the size and cost can be reduced substantially, satellite-to-home service can spread widely. Satellite-to-theatre service is at present at the conceptual stage and experiments are being carried out.

C. Cable television

Cable television generally refers to a cable-based carrier that delivers multiple programmes from a cable station operator simultaneously to subscriber households. Programmes may originate from different sources including productions from studio, from a tape or film recording, reception covering a terrestrial communication network or via satellites. The system is available and the same can be used in order to broadcast signals as they are received from other stations or those purchased by way of special services. The emergence of satellite distribution provided further impetus to expand cable network in United States and West Europe, where a very large number of households have been wired for cable reception.

In spite of the warm reception to cable television in certain countries, the system suffers from a number of drawbacks. These negative points are:

- Restricted choice in programming,
- Lack of portability, and
- Obligation to use only the operator's equipment.

Cable may, however, be acceptable as a way of facilitating small extensions to the satellite footprint or to remedy reception dead spots.

D. Fibre-optics

Fibre-optic technology makes it possible for optical fibres made of special glass to carry digital signals in the form of light pulses. This technology presents an entirely different range of possibilities in relation to speed, reliability, equality of signal, and to its relatively large carrying capacity, when compared to conventional conductors. Cables made of optical fibre that carry digital signals in the form of light pulses can prove to be the most important development in communication technology for the carriage of voice, data and video. Optical fibre networks have been laid in certain countries of the world but many developing countries still do not have the resources for installing such networks.

E. ISDN

The invention of pulse code modulation (PCM) techniques opened the way for digital transmission, whereby an analogue signal - usually in a composite wave form - is sampled and converted into a train of discrete bits. Digital techniques developed fast thereafter and the latest in this field is the integrated services digital network (ISDN) which has the capacity to cover voice, data, text and video. This would, however, require very advanced telecommunication networks and agreement on a number of protocols for signalling, interconnectivity, etc. World-wide ISDN is thus a prospect only for the twenty-first century. The system works through the telecommunication network, which includes subscriber lines (local network), the switching network and trunk network.

F. High-definition television

Another significant development in the audio-visual technology is high definition television (HDTV) which succeeded in producing on television an image as good in quality as a 35 mm film image on screen. The concept is revolutionary and can entail far-reaching changes in the production and exhibition sectors. One such change under experimentation is the transfer of video signals to film ones. HDTV technology is attracting increasing interest, and a few full-length films have been

made with HDTV equipment. The major hurdle to HDTV technology is the "line standard", which constitutes one of the important elements of principal broadcast standards - PAL, the major European standard, uses 625 lines and NTSC, the American system, uses 525. The greater the number of lines, the better the quality of the resulting picture. HDTV system uses more lines than any existing broadcasting standard, but rival prototype systems have different line standards. The Japanese have adopted a system based on 1125 lines as representing the quality obtainable with 35 mm film but this system implies wholesale replacement of equipment, wherever accepted. The competing United States standard specifies 1050 lines - twice the existing NTSC line standard and perhaps permits the use of existing receivers after conversion. Other standards from United Kingdom, France, the USSR and elsewhere conflict with these. HDTV also has the problem of signal bandwidth because of too many demands on the available space in the bandwidth as HDTV has more picture information to convey and even sound would require more space to match the new picture quality. A wholesale replacement of equipment would be opposed by those who have no manufacturing capacity of their own and, of course, supported by those manufacturing countries who will be able to take advantage of the new market. International efforts to agree on a new and universal HDTV standard have not yet met with success.

In the 1980s, the market for audio-visual products expanded enormously due to (i) the privatization of previously State-owned broadcasting in Western Europe; (ii) technological advancement, and (iii) increase in demand for entertainment products to fill in the ever-increasing airtime of commercial distribution networks including cable television, satellite television and video. A film or television programme could now be exploited, in addition to (a) theatrical, (b) non-theatrical and (c) television rights, for video, cable, pay-TV and satellite rights all over the world. This meant the generation of larger revenues from the same product. These developments made the major companies which were already dominating the world market all the more conscious about the possibilities of further expansion.

The advancement of technology expanded the scope for production/exhibition and distribution techniques and offered better options to improve quality and make much greater profits on the

audio-visual products. Technological developments related to original creation of the programme material have been on the positive side. Similarly, such developments have also brought the product nearer to the consumer. Some of the developments have contributed both to production and distribution. Video-based technologies coupled with the use of computer is an example of this variety. The scope for special effects with the use of computers which enable the manipulation of images has become unimaginably large and has provided new opportunities for film makers.

G. World trade in hardware

It has been observed that United States dominates the audio-visual field as far as media products such as films and television programmes are concerned. Asia leads in hardware and plays a dominant role on all counts - television receivers, cinematographic cameras, projectors, etc. This is due primarily to the performance of Japan and to some extent, of the Republic of Korea, Hong Kong and Singapore.

H. Video market

It is difficult to obtain data for the total number of video cassette recorders, household penetration achieved by the VCRs and total receipts generated by video software etc. for the world. Available data indicate that the global figure for total video units is estimated to have reached 200 million by the end of 1988. The penetration had exceeded 50 per cent in 17 countries and territories and 40 per cent in another nine countries by December 1987. These seventeen are: Australia, Bahrain, Hong Kong, Iceland, Ireland, Kuwait, Lebanon, Malaysia, Netherlands Antilles, New Zealand, Nigeria, Panama, Quatar, Singapore, United Arab Emirates, United Kingdom and United States. The other nine countries are: Bermuda, Canada, Cyprus, Federal Republic of Germany, India, Luxembourg, the Netherlands, the Philippines and Saudi Arabia. It needs to be noted that in some of the other countries such as Nigeria and India, the number of television sets in private homes is relatively low in relation to the size of the population. The high figures, therefore, reflect the fact that middle class homes are increasingly likely to have a video as well as a television set.

With the number of VCRs on the increase everywhere and the household penetration level nearing 90-100 per cent in some countries, the demand for programmes - feature films, television serials, mini-serials, etc. - has reached enormous proportions, and the video business has become a thriving business, overtaking movie-house business in many countries (United States, United Kingdom, etc.). There are currently more than 70 million pre-recorded tapes being sold annually. The figure for blank tapes exceeds 500 million a year.

The introduction of new technologies has substantially re-arranged the structures of communication systems and of the mass media. This process has not yet reached the first stage of equilibrium and the splintering effect that video, cable and satellite would seem to have had on the more traditional audiovisual media has yet to be charted, let alone understood. It seems, however, that this splintering effect, instead of creating the conflicts and contradictions among the media that one may expect from the play of such powerful and competitive market forces, is leading rather to new onvergences and interrelations. These convergences and interrelations seem to be mainly in the production and distribution areas.

III. PROBLEMS AND QUESTIONS

Apart from inducing the media magnates and entrepreneurs to do their best to consolidate their distributive empires, the march of technology has posed some serious questions and created certain problems, which need to be noted. Video technology has made transfer of image and sound from a film or a tape onto a blank tape child's play. Theft of audio-visual programmes and getting them onto a blank tape without due authorization from the right-holder have therefore assumed global proportions, and piracy has posed a very serious problem to governments, industry representatives and others concerned with the product. Promulgation of the Copyright Act has not solved the problem. There has been considerable thinking world-wide as to how to resolve the problems posed by piracy.

The quality and likely effects of satellite television are major issues in contemporary Europe and many other parts of the world. Depending on the orbit, altitude, power and other factors governing the

satellite's performance, the satellite has a predetermined "footprint", or reception pattern. Whatever is done to set up the pattern, it will not exactly coincide with the national boundaries of countries surrounding the country from which the satellite operates. Satellite television is thus another innovation which, along with many other factors, has caused confusion in both the production and distribution areas. Various facets of this confounding situation have been summarized by Susan Christopherson and Stephen Ball:

- Which national laws and regulations apply to a broadcasting system whose footprint covers several countries?
- If a country within the footprint wishes to opt out of the satellite coverage, how does it achieve this?
- Assuming that some kind of regulatory system can be established by mutual agreement between the affected countries, how can this be policed?
- If a sanction is brought against a satellite organization by its current host country on the basis of that country's objection to programming content, what is going to prevent the production or administrative centre being shifted to another country within transmission reach of the satellite?
- The problem inherent in the control of DBS systems might mean that corporate power is greater than national power in this area. This has significant political implications.2

All these problems have engaged the attention of various international organizations dealing with the audio-visual products.

IV. SIX SITUATIONS

At this state, it would be interesting to have a look at the position of the Republic of Korea, Japan, Hong Kong, Australia, Singapore and India in the world scenario. Some tables have been prepared in order to facilitate a better understanding of the regional situation. Tables 3-9 depict a comparative view of these countries. The major observations emerging from these tables are the following.

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2 *Ibid.*, pp. 276-77.

These six countries include India, the largest single film-producing country, and Japan, the third largest film-producing country in the world. In spite of the fact that Singapore does not produce any films, these six countries, as a group, produce 32 per cent of the world's output, which ranges from 4,000 to 4,200 films per year. This needs to be weighted against the fact that around 40 out of 65 film-producing countries produce less than 40 films per year. India, Japan, Hong Kong and Republic of Korea, producing more than 100 films each per year, are thus prolific producers. Three out of these countries, India, Japan and Hong Kong, figure in the list of nine major film exporting countries of the world. Japan is also one of the five major exporting countries of the world for television programmes.

A perusal of table 1 indicates the relative importance of exports by India, Japan and Hong Kong. It is clear that though India sells its films to fewer countries than Japan and Hong Kong, its performance in the destination countries is much better, as Indian films dominate markets in those countries to a large extent. It also demonstrates the impact of linguistic divisions, since Indian films are seen in many countries in original version, while Japanese and Hong Kong films appear only in English-dubbed versions.

Video has established itself in all the six countries. There is, however, no pay-television or any organized cable networks in any of these countries. Satellites have been installed, but they are mostly meant for the use of the owning country. Overlapping, if any, has not posed any serious problems. Direct broadcasting satellites have not entered the fray except to a very limited extent in Japan and Australia. All the countries are members of INTELSAT and INMARSAT, enabling them to receive programmes internationally.

Local production of films has a negative effect on import of films. Import is also governed by the number of cinemas, VCRs and television receivers in the country. This is why Japan imports the largest number of films and India, the least. Singapore imports a large number of foreign films because it has no film production of its own and has a high concentration of television receivers and VCRs. Republic of Korea, Hong Kong and Australia do not produce enough films to satisfy domestic demand.

United States dominates imports as 44 per cent of the films brought into the six countries are from United States, with United Kingdom, France and Italy following far behind (table 5). Imports are mainly from the American majors who formed a cartel more than 50 years ago - the Motion Picture Export Association of America (MPEAA). Hong Kong and Japan buy films from each other regularly. Fifty per cent of Japanese film exports to countries in the region are to Hong Kong. Hong Kong also sells its product to Australia, India, Republic of Korea and Singapore, while Japan sells only to Australia and India, within the group.

India has the largest number of cinemas and the annual attendance stands at an impressive 4.7 billion (table 6). United States is reported to have crossed one billion in the recent past. On a per capita basis, however, India, Japan and the Republic of Korea lack cinemas. Hong Kong and Singapore reflect excellent per capita attendance, but this may be because of the floating population of tourists. Box office receipts are maximum in Japan followed closely by India (table 7). These receipts, however, have a direct relation to the number of cinemas and the cost of admission. Japan has the highest rate at \$7.74 while India the lowest at \$0.20. It can be seen that the admission rates in turn have a direct relation to the per capita income of the country, indicating the relative paying capacity of the people of that country. Box office receipts also indicate the trend of imports for each country and the performance of foreign films in that country (table 7).

Figures for television coverage indicate practically 100 per cent coverage by 1990 as the figures given in table 8 are for 1987. For India also, the coverage has exceeded 80 per cent by now. The number of VCRs has also gone up considerably in these six countries during the three years after 1987. This indicates need for films and television programmes on an increasing basis.

On the hardware front, Japan totally overshadows all others not only in the six countries but also in the rest of the world (table 9). India is practically a non-performer in this field: not only does it not export but there is no worthwhile import inspite of its impressive film production.

All the six countries are cinema-conscious countries with a tradition of film making. The rights to be exploited most in these countries concern movie-house production, television and video. Cinema-going habit is fairly wide-spread in all of them.

A. Australia

Australia has always been active in the area of films. Intense lobbying for government intervention and assistance had begun as early as 1927 with the establishment of a Royal Commission on the motion picture industry, but little was done until some 40 years later. Australia's cultural heritage had then become a crucial issue and film was being proposed as the essential vehicle to explore that heritage. The Government of Australia manifested its positive interest in this area by the establishment of various institutions such as Australian Film Commission, Film Finance Corporation, Film, Television and Radio School, Film Australia Proprietary Ltd., Australian Film Institute, National Film and Sound Archives, etc. Positive interest in cinema was shown at the State level also, and film bodies operate in New South Wales, Queensland, South Australia, Victoria and Western Australia. All of them are funded by the respective State governments and they do substantial work to encourage local film production.

The Australian Film Commission, established in 1974, is the Commonwealth Statutory Film Authority responsible for encouraging the production, distribution and exhibition of Australian films, providing advice to the Government on film matters, monitoring developments in the industry and providing an information resource. Film Australia, a wholly owned Commonwealth Company, is the national film and video production house and acts as Government's film maker with responsibility for producing films for Commonwealth Departments and Agencies. The Film Finance Corporation incorporated in 1988 operates as specialist financing in loans and loan syndicates, guarantees, underwriting, agreements, joint ventures, etc.

Government thus takes interest in all film-related areas - production, financing, training, conservation, monitoring and regulation. Film is the responsibility of the Department of Arts, Sports, Environment, Tourism and Territories. Censorship of films exists in Australia,

but it is practised under the State laws, with co-ordination at the national level by the Attorney General.

The major source of film financing in Australia is the Australian Film Commission and Film Finance Corporation, which provide financial support if the project has Australian content and if it satisfies certain other criteria. The scheme covers feature films, documentaries, television serials, short films, etc. Apart from direct funding, the Government initiated a major step by introducing a tax incentive scheme in 1981, aimed at attracting more private investment in films. Known as Division IOBA Scheme under the Income Tax Assessment Act, this scheme allowed 150 per cent of investment as deduction and made net income from exploitation of the film tax free up to 50 per cent of the original eligible production expenditure. This led to a boom in production of feature films as well as of documentaries, but the scheme had to be amended when it was noticed that the industry was facing serious problems due to a production-bunching effect caused by the scheme requirement that film completion occurs in the year of investment. Currently, investment in eligible film qualifies for a 100 per cent deduction with all returns treated as taxable income.

Television in Australia is handled by the Ministry of Trade and Communications. Three statutory authorities have been established in Australia to administer the broadcasting system and provide broadcasting services. They are (a) the Australian Broadcasting Corporation (ABC), which provides nation-wide, non-commercial television service; (b) the Australian Broadcasting Tribunal, which licenses and regulates commercial and public television systems; and (c) the Special Broadcasting Service (SBS), a non-commercial multilingual and multicultural television service. Most of the annual budget of ABC is met from funds provided by the Government. SBS is also funded by the Government, although it is allowed sponsorships for certain programmes. ABC and SBS co-exist with privately owned commercial television networks to provide variety and choice. Up to 20 per cent investment in these three private networks can be made by foreigners and, as a result, the United States and the United Kingdom have invested in these companies. Media magnates and individual entrepreneurs like Kerry Packer, Alan Bond (Network 9) and Rupert Murdoch (Network 10) have entered the

area because of their realization that control of distribution networks is important.

The Australian Broadcasting Tribunal insists on Australian content in television programming and advertising and prescribes a percentage to be honoured by the television networks, as it has been entrusted with the responsibility of controlling the licences as well as deciding what is in the interest of the public and, in particular, of local communities. The tribunal prescribes the percentages and systems after due enquires, surveys and public debates. The tribunal has also prescribed standards for the content of children's programmes.

AUS-SAT I, II and III is the Australian Satellite operated by AUSSAT Proprietory Ltd., a Government Company, which primarily has a national coverage, apart from Papua Guinea and New Zealand. INTELSAT is used for receiving international programmes, whereas the direct broadcasting satellite is used only in remote areas.

Australia encourages co-production on international levels. This policy has paid rich dividends, and many Australian films have attracted international attention and gained recognition. Australia has Copyright Act but it has been argued that this has not effectively presented privacy.

Australia does not have any major manufacture of VCRs, video tape, or television sets. Since 1980, over 99 per cent of all VCRs used in Australia have been imported fully assembled from Japan. According to the Australian Bureau of Statistics, Australia has exported just over $2.5 million worth of VCR equipment per annum since 1983. Of this, over $1 million is exported to New Zealand. As Australia has no manufacturing capability, these exports are primarily re-exports largely from the Pacific region. It is interesting to note that the attendance in cinemas is on the increase. Total gross receipts from cinemas in Australia increased 15 per cent in 1988-89.

Video penetration of domestic households in Australia is more than 59 per cent. In 1984-85, the video distribution industry was worth some $85-89 million. The level of business has declined in recent years and reached a saturation level. Australia assesses a 20 per cent tax on

video cassette sales on the wholesale level and on royalties derived from licensing motion pictures for video distribution.

Film distribution and exhibition are handled by three private Australian companies as well as by the American majors through the MPEAA. Export of Australian films is on the increase and estimated to generate slightly more than one million dollars per year. Promotion and marketing of films is handled mostly by the Australian Film Commission which participates in the international film festivals/markets on a regular basis. Overseas offices have also been established by the Australian Film Commission to look after marketing on a day-to-day basis. Marketing of television programmes is handled by the television networks themselves by regular participation in special markets organized internationally for television and video. Australian films have an advantage in the field of exports because they are made in English, which is the most internationally marketable language for films and television. A large part of the Australian exports in film are to the United States and the United Kingdom.

B. India

India has always been a film-loving country. With its first feature film in 1913 and the first talkie in 1931, it has completed 77 years with films and film-making. As has been pointed out elsewhere, India is the largest film-producing country in the world with an output of 20 per cent of the world's production.

The Government of India has always treated film as an extension of culture and has taken many positive steps to encourage film making in the country. The major institutions established by Government for the support of its film sector are National Film Development Corporation (NFDC), Film and Television Institute of India, Films Division, National Film Archives of India, Children's Film Society of India, and the Directorate of Film Festivals.

These institutions together take care of the production and financing of films and documentaries, training, conservation and promotion. All these institutions work under the administrative control of the Ministry of Information and Broadcasting of the Government

of India. Interest in cinema has percolated to the State governments also, where State Film Development Corporations have been established in 14 States. In the remaining parts of India, cinema is handled by a department specifically named for the purpose.

The National Film Development Corporation has been designated as the canalizing agency for export of Indian films and import of foreign films. The private sector in India is very active in the area of film production/exhibition/distribution and a major share of funding comes from private parties. In the area of feature films, the private sector produces practically 99 per cent of the country's output while NFDC, a public sector undertaking owned 100 per cent by Government, is responsible for the rest. The situation is reverse in the case of documentaries where the Film Division, funded by the Government of India, is responsible for practically the entire production. Also considering films as a cultural vehicle, various State governments have prescribed quotas for screening of regional films in the cinemas in their respective areas.

It is estimated that there are 8,689 permanent and 4,462 temporary cinemas in India. Though impressive in absolute numbers, they are still not adequate in relation to the size of the population. In India, films constitute the most popular source of entertainment for the common man. This explains the impressive audience attendance figure of 4,500 million per year. NFDC as well as some of the SFDCs have devised schemes to encourage the construction of cinemas, and incentives are being offered to attract private capital in this area.

Realizing the importance of the film industry, the Government of India had appointed a high power committee to look into the problems of the industry, including problems of video piracy and cable television. The report of the Committee has been submitted and most of the recommendations have been accepted. Excise duty on prints has been abolished and efforts to induce the State governments to reduce the entertainment tax are afoot. Special funds are being earmarked for being given as loans for construction of theatres.

Television in India is State-controlled and looked after by Doordarshan, an institution established by the Government of India. The expansion of television in the 1980s has been phenomenal. For

instance, in 1983, television covered a mere 19 per cent of the population. Within a year, with the installation of 180 transmitters and by networking them to Indian satellite and microwave terrestrial links, the coverage jumped to 70 per cent. The present coverage is more than 80 per cent. Doordarshan commenced a commercial service in 1976, and from 1983 it has started accepting sponsored programmes which bring substantial revenues for the organization. Doordarshan also sponsors feature films and co-produces films with the National Film Development Corporation.

All feature films, documentaries and video films are subject to certification by the Central Board of Film Certification, which is under the administrative control of the Department of Culture, Ministry of Human Resource Development. The Board is fairly strict about the extent of violence, sex and about the treatment given to women in the films. All feature films imported from abroad have to undergo preliminary scrutiny for "quality" by a Committee appointed by the Government of India.

Video has substantially penetrated the Indian market. There has been an upsurge in the establishment of video hotels, video restaurants, video clubs, video parlours, video rooms, video theatres, etc., where VCR with a wide-screen projector is generally used for presenting films and other programmes. Video magazines have appeared presenting general news or events of interest in the film world. Video has also been utilized for the training and self-education of members of an association called Self-employed Women's Association (SEWA), a trade union for the poor. Apart from using video for political campaigning, another popular use of video technology in India is for coverage of weddings and other personal events in the family. Video is, therefore, big business in India. Though authentic figures for revenue from video are not available, it is estimated that this is several millions of rupees.

Video piracy is, however, widespread and practically uncontrolled, in spite of the stringent Copyright Act. The film industry was in serious trouble at one time because piracy had adversely affected attendance in cinemas. The situation is somewhat resolved by now and producers of Indian films have started getting good prices for video rights of their product. Nonetheless, piracy continues, affecting films,

foreign television serials, etc. as well as Indian films. With the proliferation of colour television and VCRs, cable television has begun appearing in urban centres and especially in small clusters of high-rise buildings in cities like Bombay. Much of the audio-visual products shown on cable television are of the pirated variety and without due authorization.

According to the Import Policy of the country, foreign films can be imported by the National Film Development Corporation, non-resident Indians (NRIs), private Indian parties (only during the International Film Festival of India), MPEAA and Sovexportfilm. More than 54 per cent of the imported films come from the United States. United Kingdom is the second major source of imports (18.4 per cent), followed by France and Italy (4.6 per cent each).

All importers except the NFDC are required to pay a service fee to the NFDC, the designated canalizing agency. There is no ceiling for films to be brought into the country by the NRIs, NFDC and the private Indian parties, but in the case of the last two, there is a predetermined foreign exchange allocation for the year within which they operate. No repatriation is allowed from receipts generated by NRIs' or private parties' films.

Import of films by the MPEAA and Sovexportfilm is governed by special agreements executed with them by NFDC. Under the agreement with MPEAA, they are allowed to bring up to 100 films per year and repatriate amounts specified every year. Sovexportfilm can bring up to 20 films per year without any provision for repatriation. Since Indian films are very popular in USSR, Sovexportfilm has also agreed to buy Indian films amounting to Rs. 13.5 million every year. Both of them have to pay the prescribed service fees to NFDC.

The Government encourages imports to ensure exposure of domestic audience and film-makers to diverse film cultures from all over the world. There is already a shortage of cinemas in India, and large-scale import of foreign films provoke resistance from the local industry. Indians appreciate English language films but films subtitled in English are not very popular. Films brought into India are therefore in English or dubbed in English. The total number of imported feature films in 1989-90 was 174.

Distribution of foreign film is done by the National Film Development Corporation, MPEAA, Sovexportfilm and some private distributors. Both MPEAA and Sovexportfilm have their own distribution channel system in India. The American majors have been operating in India for more than 50 years. Their operations in India have attracted criticism from many quarters, including NFDC, reportedly for various unfair practices followed by them, including abuse of their dominant position of market power by blockage of cinemas.

Export of Indian films is done by private exporters and NFDC. Indian films are very popular in certain parts of the world where they have been viewed for a long time. Countries in the Middle East have been a major destination for Indian film exports. In 1989-90, countries in the Gulf accounted for 19 per cent of film exports from India. USSR accounted for 6.6 per cent and the United Kingdom and Ireland together for 7.2 per cent. India is one of the nine major exporting countries in the world. This is because of (i) a large number of Indians settled abroad, (ii) historical or geographical association, and (iii) cultural affinity. Indian films are becoming acceptable in new territories also with the passage of time, on account of their themes, treatment and presentation. They, however, face a formidable language barrier because of the multiplicity of languages in which they are made. Whenever necessary, they are then shown in subtitled or dubbed variety. Export of Indian films generated receipts amounting to Rs. 152 million in 1989-90, and export of recorded video cassettes based on films generated Rs. 27.9 million during the same year. Thus, the total export figure stood at Rs. 179.9 million ($10.5 million). This performance has been achieved despite the video piracy rampant in most of the territories where Indian films are very popular.

Co-production of films on an international level is encouraged in India. Many such co-produced films - *Gandhi, Salaam Bombay*, etc. - have gained international recognition, besides doing very well at the box office. India has also become popular as a location for film production.

C. Hong Kong

Hong Kong is a free port which follows a laissez-faire economic policy, with minimum regulations beyond the rule of law. With an

economy which is export-oriented, Hong Kong is the third largest financial centre after London and New York. Its population of 5.7 million comprises 98 per cent Chinese, 1.5 per cent Western expatriates and less than 1 per cent other Asian nationals. The number of films produced per year in Hong Kong has been on the increase for the last few years, reaching 156 in 1989. All these films are in Cantonese Chinese and then dubbed in English for export purposes. People of Hong Kong have great interest in their films, indicated by the per capita attendance in cinemas. As already pointed out, Hong Kong is one of the major film-producing countries in the world. Under the Film Censorship Ordinance, all films have to pass through the Censor Establishment. There is a withholding tax of 1.65 per cent of profit on an imported film. In 1983, Hong Kong imported 429 films, the United States being the source of 28.4 per cent of them. Japan accounted for 8.2 per cent and the Federal Republic of Germany for 7.7 per cent.

Television Broadcasting Limited (TVB) started broadcasting in 1967. TVB became a publicly listed company in 1984. Asia Television is the other television network with two major shareholders. Both these Networks have two channels each, one in English and other one in Chinese. Television is very popular in Hong Kong with practically every family having at least one television set. Radio-Television Hong Kong (RTHK) is a government-funded organization. RTHK produces both programmes of general interest and educational programmes in the form of documentaries, drama, magazines, variety and game shows, etc. Particular emphasis is given to the areas of current affairs and civic education. These programmes are transmitted on all four channels of TVB and ATV under an agreement with the Government. The television networks are controlled by the Broadcasting Authority of Hong Kong, which is a statutory body. TVB International is an arm of TVB for international operations.

Video is also very popular in Hong Kong. The household penetration is high. Like in India, video is used in many ways to communicate with people on different subjects - entertainment, educational, promotion, training, etc. Distribution of films is entirely in the hands of the private sector. The private sector comprises Hong Kong companies as well as regional offices of MPEAA which handle their own product.

Hong Kong is one of the nine major exporters of the world. Films made in Hong Kong in Cantonese Chinese language are in demand in Southern China, Canada and Australia where the resident Chinese speak this language. Hong Kong's action film dubbed in English are also popular in many parts of the world. Hong Kong encourages co-production. Hong Kong is also popular as a location for film production.

Hong Kong had its Satellite, ASIA-SAT 1, launched in 1989. The satellite is owned by three partners, one private party from Hong Kong, a foreign party and the Chinese Government, each holding equal shares. The intention is to cover Hong Kong and the adjoining mainland to a certain extent. There is no direct broadcasting satellite (DBS).

Cable networks do not exist in Hong Kong. Cable is, however, expected to be operative by 1991. Franchise for cable operation has recently been given to Hong Kong Cable Communication, a private company, on an exclusive basis. Difficulties and technicalities arising out of this situation vis-à-vis ASIA-SAT 1 are being sorted out. Hong Kong does not produce any VCRs. Blank cassettes are produced as are parts for assembly, by a number of small family business in Hong Kong. Other cinema-related hardware is mostly assembled and exported. Imports, however, are much larger than exports. In 1984, the VCR export and re-export was estimated at HK$336.2 million, while imports amounted to HK$2222.1 million. The export figures for blank video tapes for the same year were HK$598.3 million and HK$688.3 million respectively. Trade in pre-recorded videotapes was of much smaller volume (HK$29.4 million exports and HK$18.5 million imports in 1984).

D. Japan

Film making started in Japan in 1910 and it was the biggest producer of films in the world for quite a few years. The industry began to flourish again in the post-war period; and remains the third largest film producer in the world, its second position having been taken by United States for the last few years. Japan is also one of the nine major film exporting countries in the world. It has the distinction of being one of the five major exporters of television programmes also. In ad-

dition, Japan is the acknowledged world leader in cinema-related technology.

Though cinema is very important to the Japanese, the number of films and cinemas as well as the annual attendance therein has been coming down noticeably. In 1989, Japan produced 255 films, while the average film production during the decade has been 306 films per year. The number of cinemas in Japan in 1989 was 1,912, showing a 4.6 per cent decrease compared to the previous year. This is primarily due to the increasing use of video cassettes in Japan. In 1988, the cinema industry showed a distribution profit of some 325 billion yen (some ($260 million), while the profit from video cassette sales was three trillion yen ($ 2.3 billion). In Japan, the video-cassette industry is being hailed as the new "film" industry: a major structural transformation has occurred. Film production has by now, as never before, become a part of the industrial complex.

Realising that the local industry needed help, a report concerning the promotion of film and arts has been prepared and the Government is seriously considering grant of aid for film production. It is expected that this will be 25 million yen per film per year for 10 feature films; five million yen per film per year for five short films, and five million yen per film per year for animation films. This is expected to be in addition to the present cash awards of 10 million yen per film to 10 selected Japanese films every year.

In Japan, all the sectors of the industry - production, exhibition and distribution - are in the hands of the private sector. Even the video industry is run entirely by the private sector. There is no organizational structure in the Government to overview the industry except the Ministry of Trade.

Japan has a voluntary censorship board, the Motion Picture Code of Ethics Commission (EIREN) consisting of local and foreign distributors, to review both imported and domestic films in a liberal and enlightened manner. EIREN has very rarely banned a film but it may suggest slight cuts. There is a customs examination which takes note of what might be classified as pornography and indicates to the importer or EIREN what should be done in such cases.

Japan became a free market for film imports in 1964 and there were fears that a glut of imported films would have an adverse effect on the already ailing local industry. Rather than face legislation imposing a quota of film imports or a law controlling showings of imported films, the industry decided to voluntarily adhere to a suggested screen-quota system which includes a stipulation that all cinemas devote a certain number of days every year to screen domestic films. Certain cinemas devoted to showing only imported films have, thus, to keep apart 40 days a year to showing domestic films of good quality. A withholding tax of 10 per cent is charged for every imported film in Japan. Foreign films are a mainstay of the Japanese business. Japan is the largest market for United States films. They accounted for 48 per cent of the films imported to Japan in 1989. Italy and France are the other major sources of import, accounting for 13.7 per cent and 12.3 per cent respectively.

Distribution and exhibition in Japan is mostly in the hands of the private sector. The private sector again comprises major and minor Japanese companies as well as MPEAA. As in other countries, MPEAA companies have chosen not to operate individual offices but to function by joint efforts through two or three individual companies. As regards exports, the Japanese films are shown abroad with subtitles or in dubbed version. The big houses in Japanese film industry participate regularly in the international markets held at different places in the world in order to promote and market their films and television products. For the past three years, France has overtaken the United States as the most prominent destination for Japanese film exports. In 1989, France received 24.3 per cent of Japanese film exports, followed by the United States (16 per cent) and Hong Kong (10.4 per cent).

After the Second World War, commercial broadcasting was introduced in Japan to encourage freedom of speech and stimulate the process of an increasing exchange of information. Television expanded very rapidly - based upon an equally rapid economic growth - and this enabled the Japanese people to view a far wider range of media products. There are at present two types of broadcasting organizations in Japan - two public broadcasting corporations and 102 commercial broadcasting companies. One of the public corporations - Nippon Hoso Kyokai (NHK) - is financed via an annual licence fee, and the

other - the University of the Air - is owned by a government-funded corporation. NHK has two nation-wide networks covering the whole of Japan and about 90 per cent of all programmes are produced in Tokyo. The commercial companies are financed through sponsored advertising and there are one minor and four major networks. NHK is also trying out high-definition television (HDTV) on an experimental basis for which 100 special sets have been specifically given all over Japan.

There is no cable television on a national level in Japan. Some cable television stations, however, feed to 4.3 million households where television reception is poor or non-existent. In the cities, cable television is piped to hotels and to some high-class appartments. In suburbs, some multi-storied housing complexes have their own cable television. Piracy is a serious problem in spite of the Copyright Act and the establishment of the Federation Against Copyright Theft for Japan (J-FACT) by the industry to fight video piracy.

Japan has already been described as the pioneer and leader in cinema-related technology. Its role is not restricted only to manufacture and sale of equipments; it has also earned a name for itself for research and development work. Japan has also evinced interest in co-production of films with international producers. This has paid rich dividends.

E. Singapore

Singapore began making movies as early as the 1930s, using technicians imported from Shanghai and local Malay actors. Apart from Malay, films were also made in English, Chinese dialect, Tamil or Hindi. Two private parties were very active and the production was about 12 films a year. Films continued to be made in the 1950s and 1960s also. Film production, however, faded out and stopped altogether after 1975. The City State, however, has a fairly large number of cinemas and attendance is very high. Singapore has a Board of Film Censors established under the Cinematograph Ordinance, 1953 and all films - imported films, commercial advertisement films, etc. - need Censor approval before they can be screened anywhere.

Singapore depends entirely on imported films for supply of films to cinemas. The United States is the most important supplier (41.5 per cent in 1989), followed by Hong Kong (33 per cent). There is no restriction on the number of films for import or on repatriation of money thereof. Distribution of films is done by private parties including the American majors, who have set up their offices in Singapore.

Television entered the Singapore market in 1963, when a pilot monochrome television service of one and half hours was introduced. Colour television came 11 years later when transmission began in 1974. The Singapore Broadcasting Corporation (SBC) was established in February 1980 to allow for greater autonomy in finance and management matters. The Corporation also licenses and regulates the sale and use of television receivers and broadcasting apparatus. The rising number of licences issued each year is indicative of the public's dependance on television as a source of news, information and entertainment. In 1987, there were 560 million television receivers in use in Singapore, showing an increase of more than 40 per cent over the figures for 1980.

SBC works through three channels - channels 5, 8 and 12 - catering to various language programmes. SBC produces nearly 40 per cent of the programmes telecast while the remaining programmes are acquired from overseas. SBC has set up its own commercial arm, SBC Enterprises, for handling sale and marketing of its programmes abroad. Singapore has a Copyright Act and the Governments is strict about its compliance. The country does not have any satellite and there is no cable television except closed-circuit television in some hotels.

Singapore has, however, made certain interesting announcements recently. The Government has stated that they aim to transform Singapore into a film centre for the South-Asian region. The Economic Development Board in charge of investment in Singapore has been asked to find ways of meeting the creative manpower needs of the film, advertising, media, television and video industries. The following ten years have been described as the "Decade of Creativity". Many developments have taken place in the light of this new policy. A high-powered committee is working hard to establish an infrastructure that will attract film-makers from all over the world by offering generous fi-

nancing, relaxed censorship and sophisticated production facilities. Italian film moghul, Cecchi Gori, has plans for a $34 million movie-making facility along the Tuas shoreline and construction is expected to start early next year. Golden Harvest Group from Hong Kong has plans to build a multiplex cinema. Another project, Tang Dynasty Village, which will also house a film studio, is scheduled for completion in mid-1991. The Government has also announced the establishment of a fund to promote movie and video concerns and S $300,000 worth of scholarships for promising young talent.

F. Republic of Korea

The Republic of Korea is another country which has always taken positive interest in cinema. The Motion Picture Promotion Corporation, an incorporated body, was founded as a non-profit organization in 1973 by the Government under the film law. The MPPC has been entrusted with the overall promotion of films in Korea and, in that capacity, supports the Korean Film Archives, operates the Korean Academy of Film Arts, promotes and markets Korean films abroad, imports foreign films and supports the Korean film makers. The MPCC does not itself produce films but finances film making and gives cash awards to a selected number of films every year. The Corporation also supports and hosts international and domestic film festivals.

The number of films produced in the Republic of Korea has been fairly large, with a noticeable increase in 1989. The country produced 110 films in 1989 - 26 per cent more than the previous year. The number of cinemas has also been showing an upward trend for a number of years (10.9 per cent increase in 1988-89), resulting in better attendance in the theatres.

Films are subject to censorship by the Public Performance Ethics Committee, which is strict about the extent of violence and sex in films. The procedures for review of foreign films by this Committee are under examination. All cinemas have to observe screening quotas according to which 146 days out of 365 in every theatre have to be reserved for Korean films. The admission rates are prescribed by the Government and they are higher for foreign films.

Import of foreign films is permitted but the importing party has to pay an interest-free deposit of 50 million won to the MPPC before the film is registered. There used to be a subsidy from the Korean Film Fund in the past but it has been abolished and replaced by the interest-free deposit. The customs duty is 400 won per metre. There is a higher rate of income tax for foreign films. There is also a federal tax at 10 per cent of the royalty.

Films are imported from 18 different countries but the major source is the United States, followed by Hong Kong (a close second), Italy and France. Foreign films were always imported by registered Korean companies in the past and distributed also by the Korean firms. This, however, became an issue of dispute between the United States and the Republic of Korea, which agreed to amend its policy and allow the United States open access to the Korean market by having their own offices in Korea and distributing their films themselves. This has caused resentment amongst the local industry and the film-makers. Korean film-makers launched a nation-wide movement to "block the landing of foreign films on Korean soil".

The Korean Broadcasting Service (KBS-television) was established by the Government in 1961. This was followed by the commercial Munwah Broadcasting Company (MBC) in 1969. The American Forces Korea Network (AFKN-TV) was also established to serve American military personnel stationed in Korea. KBS, which is 100 per cent government-owned, collects a monthly fee from each household with a television set and also accepts commercial advertising. KBS has three channels while MBC has one channel. Both these networks have their own marketing divisions for overseas operations. Video has penetrated the Korean market, and 20 per cent of the households have VCRs. Video piracy, however, is widespread.

The Republic of Korea does not have a satellite and there is no cable television in the country. Although on the whole Korean films are not widely exported, 30-35 films are sold every year, worth around \$0.5 million, mostly to Taiwan, Japan, Hong Kong and Europe. Korean films also face a formidable language barrier as far as exports are concerned. They are, therefore, screened in subtitled or dubbed versions.

V. COMMON ISSUES

It is an established fact that the United States' media totally dominate the world as the major suppliers of films, television programmes and video products. The American majors constituting the MPEAA have enjoyed this dominant position for more than 65 years. They began internationalizing distribution in the 1920s and intensifying internationalization in the 1950s by modifying film content as well as through processes of co-production and inter-investment with foreign firms. Some of the majors - Paramount and MGN - operated in global markets when many goods-producing companies were just beginning to explore expansion into the foreign markets. At present the MPEAA member companies have offices in not less than 50 countries in the world.

The most significant factor which contributed to the success of the majors was the control they exercised over the distribution of films. Other American companies called American Indies, which are not members of MPEAA, also felt major's domination and established American Film Market Association (AFMA) in the early 1980s in order to look after their own interest.

The domination of the majors has been seen in many countries as constituting a barrier to their entry into the world market. It has been felt that these countries could export their product much better and even earn more in their own countries if the market were not dominated to such an extent by this cartel. The market domination appears also to operate on the import side, as countries wishing to import from countries other than the United States have found this difficult because of the market power of MPEAA.

It has been contended in some quarters that market forces alone are not sufficient to account for the dominant position of United States media products and that American multinational corporations have been instrumental in aiding this process by controlling media trade flows. It has also been contended that American domination of trade in media products, in turn, is complementary to the foreign policy objectives of the United States Government, as United States films and,

more importantly, television programmes, serve to influence public opinion in other countries and to promote American values and products in developing countries.

As already pointed out, media services have now a much larger scope to generate revenues which may run into billions of dollars. Being conscious of this capacity and noting that resistance from other countries is on the increase, the MPEAA has been instrumental in encouraging unilateral action by the United States (under Section 301 of the Trade Act of 1974, as amended). The MPEAA apparently filed complaints against Brazil, Colombia, India, Indonesia, the Republic of Korea, and Taiwan, Province of China regarding denial of fair and equitable market access to United States distributors of theatrical motion pictures, television programmes and home video material.[3] The contention of MPEAA reportedly seems to be that the media products should be treated as products equivalent to any other tradable good or service. They have, thus, taken a purely commercial view of the possibilities of films, television and video. It is as if they have totally dismissed the notion that films, television and video can have any other purpose or potential other than entertainment.[4] Recently, 33 United States senators have signed a letter addressed to the United States Trade Representative, urging that no "cultural exceptions" be included in the multilateral framework.

A. Media products and culture

It is very difficult to accept the proposition that media products are only for entertainment and that they are equivalent to any other tradeable good or service. A film, a television programme or a video show educates, trains, informs and entertains. While doing so, it also perpetuates the culture and values of the producing country, in subtle ways. In the process, the media products also influence public opinion, attitude and value judgement.

3 MPEAA spokesmen have been quoted as justifying their approach in the following terms: "Countries are like people; sometimes they won't act unless they know you can hurt them." *Ibid.*, p. 296.

4 *Ibid.*

Once it is understood that a media product is culture-related, the desire of every State to encourage its own industry by offering various incentives is justifiable on a different level altogether. While offering incentives and direct help to its own film industry, the State then also wants to ensure that the import of media products is allowed with certain reservations. The State also decides what role it should play in providing services or in representing the society's interests with respect to the quality and kind of services to be made available to its people. This is a right every State must enjoy. This is the policy that is being followed not only in the six countries and territories covered by this paper but all over the world. Various steps devised by the Governments of Australia, India, Hong Kong, Japan, Singapore and the Republic of Korea for promoting media industry in their respective areas and for receiving imported products can be appreciated in the light of this background.

B. Application of the multilateral framework

I would, therefore, conclude discussion on this point by stating that if media services are to be included within the multilateral framework, "culture" must be insisted upon as an exception. It is interesting to note in this connection that the motion picture industry is the only "service" sector already included within the framework of both the General Agreement on Tariffs and Trade and the OECD Code of Invisibles. Article IV of the General Agreement specifically permits the establishment or maintenance of film screen quotas to guarantee that a minimum percentage of total screen time will be applied to the exhibition of films of national origin. This exception to the general principle of non-discrimination is also recognized explicitly in article III (10) - the national treatment provision - which is so important to the usefulness of the General Agreement.

The OECD Code of Invisibles also contains numerous exceptions to the general principles of trade liberalization for motion pictures. Annex IV to Annex A of the Code specifically allows these exceptions, holding that for cultural reasons, systems of aid to the production of printed films for cinema exhibition may be maintained provided that they do not significantly distort international competition in export markets. The cultural implications of the media sector give it a

special character which has also been recognized in the recently negotiated Canada-United States Free Trade Agreement. In the Mid-Term Review Decision in Montreal, it has again been recognized that exceptions could be based on cultural policy objectives. Cultural exceptions would not inhibit countries from negotiating specific market access concessions for subsectors of media services. The extent to which these concessions would include national treatment would depend upon the peculiarities and requirements of each country.

In the granting of commercial presence, however, certain important factors have to be taken into account. The need to be present in foreign markets was less significant when trade in media services was largely confined to cinemas. As the possibilities for the distribution of media have multiplied, transnational firms with interests in a range of media want the right to establish and control their own distribution outlets in order to maximize their managerial control over product. Transnational distributors also want the ability to own directly or to control exhibition outlets in order to decide strategically the release patterns across markets, both increasing profits and reducing parallel imports of pirated films and cassettes.

If the right to establish distribution outlets in world markets is obtained, it is likely to result in vertical integration of production resulting in further domination of media markets by a few firms. This will also result in loss of even that small multiplier effect which is associated when exhibition outlets belong to the nationals. Another likely effect is the tendency of the distributors/exhibitors to favour their own products thus limiting the variety of products offered to local buyers.

VI. LIBERALIZATION OF MEDIA TRADE AND DEVELOPMENT POTENTIAL

I would now like to comment on the development potential arising out of trade liberalization. It has been claimed that trade liberalization will have a three-way impact. The first is that, liberalization will provide developing countries with various inputs at cheaper prices. Films and television programmes, however, are finished goods and not inputs; they are merely distributed in developing countries. There is no

technology transfer or job training in business management skills and as a result the economic development implication is negligible. It is also claimed that developing countries can provide the same skills as the developed countries but at lower costs. This claim, however, is not substantiated, since in the media industry the vast majority of the high-skilled jobs are associated with production activities which are totally concentrated in and around certain cities in the world. It has also been claimed that the developed countries will be forced to open their doors to imported services if trade is liberalized. This does not seem likely because in case of media industries practically all developed countries technically have an open market for media products from any corner of the world. The barriers that restrict entry to the markets in developed countries such as the United States are economic rather than regulatory.[4]

A. Export of Asian films: Problems faced

So far, Asian countries have operated individually as far as export of their films is concerned. Very few of them have worked consistently on the international market to make a mark for themselves. Some of the major problems faced by these countries are the following:

- *Geographical, political or economic isolation of individual countries:* Some of such countries have a substantial film production of their own, but they seem to be oblivious of other possibilities due to one reason or other.

- *Language barriers:* Asia is multi-lingual, and some countries have several languages within their own areas. Quite a few of these languages are alien to the world markets. Films produced in these languages need to be presented to the rest of the world in subtitled or dubbed versions. This involves investment which the producers do not feel confident about. Market-conscious countries have, however, started putting in this money to their advantage.

- *Domination of some foreign companies because of their long-standing operations on the international front:* As explained

5 *Ibid.*

above, the audio-visual world is totally dominated today by the American majors. Films from other countries including those from Asia find it very difficult to get playing time in cinemas. They also find it difficult to enter the television or video market due to the same reason.

- *Video piracy:* This has become an international menace as it has not been possible for any country in the world to eradicate it totally. Asian films have been losing substantial revenues because of piracy. This is, however, an area where all nations in the world have to think together and devise means to see that piracy is at least brought under control. Many international organizations, e.g. World Intellectual Property Organisation (WIPO), International Federation of Film Producers' Associations (FIAPF), International Federation of Phonogram and Videogram Producers (IFPI), etc. are active in this field. It should be recalled that Asian developing countries have supported the idea of an anti-piracy/anti-counterfeiting code in the context of the Uruguay Round negotiations on trade-related aspects of intellectual property rights.

- *Quality consciousness:* Many Asian countries have not developed quality consciousness to an adequate degree, whereas quality considerations are inescapable at every step - production, prints, subtitling, dubbing, publicity material and so on. Even if the contents have quality, if the print quality is not good or if the film does not have the requisite technical standards, this can significantly reduce the marketability of the film.

B. Possibilities for improvement

Let me now turn my attention to the possibilities for Asian countries in increasing foreign exchange earnings from the media service industry. Some of the measures that can be considered to improve performance on the export front are discussed below.

As already stated, out of the six countries, India, Japan, Hong Kong and the Republic of Korea are prolific film producers. India, Japan and Hong Kong figure in the list of nine major film exporters in

the world. Besides this, Japan is one of the five major exporters for television programmes. All these countries, thus, already have an established base of production and export from which they can take off and improve their performance further. Except for Australia, which produces films in the English language, other countries in Asia have their production in different languages which are not as acceptable as English, in the rest of the world. These countries may, therefore, select some of their already produced films for dubbing in English. The markets available for their films so dubbed in English will be wider. Depending on business judgement, they should also dub selected films in French or Spanish to expand coverage of international markets further. These three languages - English, French and Spanish - are being suggested since they cover practically the entire international market except countries where all acceptable films are dubbed by them in their own language in any case. Some films should be specially selected, depending on business judgements, for bilingual production, right from the beginning. Though initially this will involve a larger investment, subsequent returns from the enlarged markets would justify this step.

Greater attention should be paid to the possibilities of co-production by the film makers, producers and governments. Co-production intrinsically are bilingual and ensure interest of the foreign co-producers in widening the scope in the international markets, including that in his own country. Co-production can be within Asian countries or beyond the Asian Region. Conscious efforts should be made by all countries in Asia to buy and sell films from and to one another. While it may be true that for various reasons (historical or political), these countries have generally been buying and selling films from and to different countries other than in Asia, there is enough scope to inculcate a regional affinity and to encourage consumption of the film product between themselves. It must be remembered that all these six countries under report themselves have cinemas, television and video established within their areas. The demand for films and television/video programmes in Asia is, therefore, on the increase and the same can be tapped fruitfully if conscious efforts are made. The Asian market is actually the most important market for films (30 per cent) and even for television and video, it constitutes an important segment in the world.

Recognizing need for joint efforts, the 12 countries in Latin America signed the Latin American Agreement on Cinematographic Integration in October 1989. This was done by them in order to confront the problems relating to the production, distribution and exhibition of films from the region, jointly. Recently with the signalling of the Single European Market in 1992, the Commission of the European Communities has taken a series of steps to strengthen European media production industries. In October 1989, the Council of the European Communities adopted a directive to implement the European Convention of Transfrontier Television. Reportedly, the European Commission has taken a decision to allocate $276 million over five years as seed money for audio-visual projects. This is reported to be more than seven times the current level of funding. Steps are also being taken to reduce the barriers to inter-European exchange of programmes and to inter-European co-productions. In short, the intention is to produce a much more competitive European audio-visual industry which already constitutes within itself a sizeable international market.

Countries in Asia would be advised to consider regional integration efforts in order to strengthen their media services sector. These countries should be able to take advantage of their production base and of the substantial international market possible within the region. An organization like the Economic and Social Commission for Asia and the Pacific (ESCAP), established by the United Nations for the initiation of various schemes in the Asia and Pacific Region, can be entrusted with the responsibility of over-viewing the steps devised for this endeavour. A fund should be created by ESCAP to develop movie activities within the Asian region as well as to provide as seed money to worthwhile projects.

There is sufficient scope to stimulate and increase the buying and selling of films and other products within the Asian region itself. Strategies can specifically be planned for extra-regional exports. Arrangements should be made to ensure free circulation of Asian personnel in the region for purposes of work and training, whether for short or indeterminate periods, with recognition of their qualifications. This will induce talent to remain and continue working in the region. The regional productions and co-productions could be given national treat-

ment or preferential treatment in market access, such as screen time in theatres or on television.

Efforts should be made to have a satellite covering the Asian region and then to create Asian audio-visual space with the help of that. The information technique of the next century would definitely use fibre-optic systems for transmission purposes. Countries without these grids or without policies for creation are likely to be left far behind as the technology progresses. The Asian countries need to take conscious note of this and devise suitable steps to face the challenges and needs of the twenty-first century. Technology has opened up new outlets for the development of media services. This opens up possibilities also for Asia-Pacific countries to enhance their service capacities as well as to increase their exports.

Box 1

AUDIO-VISUAL SERVICES IN THE URUGUAY ROUND

The consideration of the audio-visual sector began relatively late in the negotiation, the first meeting dedicated to this sector taking place in August 1990 at the request of the European Community. Negotiations in this area are influenced by four main considerations: (a) the extremely dominant position of the United States in trade in cinema and television programmes, and the dependance of the United States film and television industry on export markets; (b) the widespread practice of most countries to restrict presentation of imported programmes for motives relating to the preservation of cultural values; (c) technical advances such as satellite TV broadcasting, high-definition television and expanded cable TV networks, particularly in Europe; and (d) "Europe 1992" and the "Television without Frontiers" initiative, which should result in broadcasting preferences in favour of EC material in all EC member states. [a]

As a consequence, the discussions in the Uruguay Round have focused on the issue of preservation of cultural values. The United States as would be expected has strongly opposed any exception that would permit the restriction of trade in audio-visual services for cultural reasons, whether as a general exception in the overall framework or in any sectoral annotation. Most other countries recognized that the cultural issue was of crucial importance in this sector and would have to be taken into account in negotiating any liberalization commitments in trade in audio-visual services, but they had different views on how to deal with the issue in the multilateral framework. Some were in favour of drawing up a particular sectoral annotation which would provide for a liberalization in this sector while recognizing the legitimacy of policy instruments aimed at preserving cultural values. The EC subsequently submitted a specific proposal in this respect.

Some other countries recognized the legitimacy of cultural conservation, but considered that this could be covered by reservations in the schedules and not require a separate sectoral annotation. Certain other countries, including Canada, considered that cultural aspects extended beyond the audio-visual sector and should be dealt with through a general cultural exception to the framework itself. It should be borne in mind that Canada was successful in excluding "cultural industries", a much wider concept, from the Canada-United States Free Trade Agreement. [b]

The public nature of this sector, its close link with telecommunications sector and its coverage including production, distribution and diffusion were also discussed. Concerning the application of principles and concepts, problems were highlighted with respect to the strict and immediate application of MFN, market access, and national treatment because of existing co-production and other relevant bilateral agreements. Temporary movement of personnel, access to distribution channels and removal of restriction on foreign ownership were also seen as relevant for achieving more liberal market access. On increasing participation of developing countries, the issues of transfer of technology, training of personnel, and access to distribution channels and information networks were again highlighted as being of particular concern for developing countries.

a For a detailed discussion of these issues see Susan Christopherson and Stephan Ball, "Media Services Considerations Relevant to Multilateral Trade Negotiations", in UNCTAD, *Trade in Services. Sectoral Issues* (United Nations Publication, UNCTAD/ITP/26), pp. 249-308.

b Peter Burn, "Professional Services and the Uruguay Round: Lessons from the Canada-United States Free Trade Agreement", in *Ibid*., pp. 365-405.

Table 1

DISTRIBUTION OF SALES OF FILMS BY NINE MAJOR FILM-EXPORTING NATIONS

	Number of countries distributed in	Number of countries in which sales are number 1 source	Number of countries in which sales are 1 or top 3 sources	Number of countries in which sales account for at least 5 per cent of imported films
United States	78	59	78	78
France	68	-	40	39
Italy	70	2	25	34
India	47	9	24	24
USSR	57	13	19	23
United Kingdom	65	-	22	29
Fed. Rep. of Germany	56	-	8	11
Japan	55	-	5	4
Hong Kong	56	1	13	21

Source: UNESCO, *Statistical Yearbook, 1990* (Paris, UNESCO, 1990).

Table 2

EXPORT OF FILMS IN 1985 BY GROUP OF COUNTRIES

Group of countries	*Value (in million dollars)*	*Percentage to world total*	*Major countries exported to*
1. Africa	1.2	0.7	United Kingdom (44%), France (17%), Côte d'Ivoire (11%)
2. North America	61.5	36.7	United Kingdom (17%), Rep. of Korea (10%), Spain (9%), Venezuela (8%)
3. South America	2.7	1.6	United States (33%), France (24%), Spain (11%)
4. Asia	13.9	8.3	Thailand (20%), Rep. of Korea (13%), Hong Kong (12%)
5. Europe	86.9	51.9	Fed. Rep. of Germany (14%), France (12%), United States (11%)
6. Oceania & the Pacific	1.3	0.8	Rep. of Korea (27%), United States (16%), Singapore (15%)
World total	167.5	100.0	

Source: UNESCO, *World Communication Report* (Paris, UNESCO, 1989).

Table 3

IMPORT OF FILMS IN 1985 BY GROUP OF COUNTRIES

Group of countries	*Value (in million dollars)*	*Percentage to world total*	*Major countries imported from*
1. Africa	10.1	5.3	France (33%), United Kingdom (21%), United States (14%), Israel (13%)
2. North America	49.8	26.4	United Kingdom (28%), Rep. of Korea (14%), Italy (13%), United States (12%)
3. South America	11.0	5.8	United States (65%), Italy (9%), United Kingdom (8%), France (8%)
4. Asia	29.2	15.5	United States (36%), Hong Kong (19%), United Kingdom (16%)
5. Europe	82.0	43.4	United Kingdom (33%), United States (23%), Italy (11%)
6. Oceania & the Pacific	6.7	3.6	United States (64%), United Kingdom (19%)
World total	188.8	100.0	

Source: UNESCO, *World Communication Report* (Paris, UNESCO, 1989).

Table 4

FILM PRODUCTION AND IMPORTS

Country	*Year*	*No. of films produced*	*No. of films imported*	*(year)*
1. Australia	1989-90	35	250	(1988)
2. Hong Kong	1989	156	429	(1983)
3. India	1989	781	174	(1989-90)
4. Japan	1989	255	520	(1989)
5. Rep. of Korea	1989	110	264	(1989)
6. Singapore	1989	-	448	(1989)
Total		1,337	2,085	
World (estimate)		4,040		

Source: Various documents.

Table 5

SOURCES OF IMPORT

Imported from	Australia	Hong Kong (1983)	India	Japan	Rep. of Korea	Singapore	Total	Per cent
United States	204	122	95	289	91	199	1,000	44
United Kingdom	37	21	32	16	5	27	138	6
France	15	22	8	45	14	-	104	4
Fed. Rep. of Germany	3	33	1	12	7	-	56	2
Italy	23	29	8	40	30	1	131	6
Hong Kong	88	-	2	15	89	123	317	14
Japan	34	35	1	-	-	-	70	3
Taiwan, Prov. of China	17	-	-	-	-	25	42	2
Canada	9	-	1	6	-	-	16	1
USSR	18	2	5	10	2	-	37	2
Others	36	165	21	52	26	79	379	16
Total	484	429	174	485	264	454	2,290	100

Source: Various documents.

Table 6

CINEMAS, 1989

Country	No. of cinemas	No. of cinemas per million population	Population per cinema	Annual attendance in cinemas (million)	Per capita annual admissions to cinemas
1. Australia	772	45	21,049	39.80	2.4
2. Hong Kong	120	23	43,333	70.09	13.5
3. India	13,151	17	62,155	4,700.00	5.7
4. Japan	1,912	16	64,095	143.57	1.2
5. Rep. of Korea	772	18	55,699	52.23 (1988)	1.2
6. Singapore	72	27	37,361	35.78	13.3

Source: Figures drawn from various documents.

Table 7

BOX OFFICE RECEIPTS, 1987

Country	Theatre receipts (million dollars)	Percentage of national films in receipts or attendance	Average admission price (dollars)
1. Australia	131.39	10.01	4.15
2. Hong Kong	206.76	na	2.95
3. India	925.78	80.00	0.20
4. Japan	1,114.87	48.07	7.74
5. Rep. of Korea	96.72	27.00	1.99
6. Singapore	77.28	-	2.16

Source: Various documents.

Table 8

TELEVISION AND VIDEO, 1987
(Year 1989)

Country	No. of TV trans-mitters	No. of TV receivers (in 1,000)	No. of VCRs (in 1,000)	Population per TV receiver	Percentage of population coverage by TV
1. Australia	392	7,800	2,800	2.1	98
2. Hong Kong	na	1,350	750	4.2	99
3. India	174 (1985)	5,500 (1987)	1,245	142.1	76
4. Japan	16,275	31,500	17,000	3.9	99
5. Rep. of Korea	783	8,200	1,000	5.1	99
6. Singapore	3	560	350	4.7	99

Source: UNESCO, *Statistical Year Book 1990* (Paris, UNESCO, 1990), various other documents

Table 9

EXPORT AND IMPORT OF CINEMA-RELATED ITEMS BY THE SELECTED COUNTRIES, 1985

(In million dollars)

Country	Cinematographic cameras, projectos, etc. Export	Import	Television receivers Export	Import
1. Australia	4.5	153.3	0.6	46.8
2. Hong Kong	24.7	184.7	69.5	263.1
3. India	0.1	1.6	Negl.	0.4
4. Japan	3,095.6	109.9	2,802.5	8.3
5. Rep. of Korea	17.9	75.7	589.0	5.6
6. Singapore	25.6	49.4	308.3	141.4
Total	3,168.4	574.6	3,769.9	465.6

Source: UNESCO, *World Communication Report* (Paris, UNESCO, 1989); Monthly Statistics of Foreign Trade of India, Vol I and II, March 1986; Directorate General of Commercial Intelligence and Statistics, Government of India (Conversion rate used 1 US$ = Rs. 12.24).

ASEAN INTERESTS IN AIR TRANSPORT SERVICES IN THE URUGUAY ROUND

*Christopher Findlay and Peter Forsyth**

INTRODUCTION

The ASEAN airlines have achieved spectacular growth rates as suppliers of air transport services. Their shares of world output in this industry have risen as a result. In this paper, we review the origins of their competitiveness in this industry and the barriers to their opportunities to exploit that competitiveness. These barriers arise from the nature of the regulation of international trade in this service. We outline recent developments in global air transport markets and discuss the relevance of GATT principles and procedures for managing the adjustments required.

In the following section, we present a brief outline of the characteristics of the global industry. We then review the nature of the regulatory system and outline recent developments in the market place. The following sections contain an analysis of the determinants of competitiveness in the industry. We then apply this analysis to the implications of the creation of a unified market for air transport in Europe. The last sections review the applicability of GATT processes to this industry.

I. CHARACTERISTICS OF THE INDUSTRY

Scheduled traffic accounts for about 90 per cent of the total international air traffic, and charter flights account for the remainder.

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Passenger traffic accounts for nearly three-quarters of all scheduled air traffic. Since 1978 total traffic has grown at about 6 per cent a year. Freight traffic has grown slightly faster, at 7 per cent a year. The rate of growth of airline traffic is considerably faster than that of real GDP, which grew at less than 3 per cent a year in industrial market economies, and at less than 4 per cent a year in developing economies, on average over the same period. Overall, the mix of activities in terms of either scheduled versus non-scheduled, or passengers versus freight, has changed little over the decade.

Total passenger traffic is divided about 50:50 between international and domestic journeys. Scheduled services account for about 90 per cent of passenger transport, but non-scheduled services are much more important on international routes. International transport of freight by air is more important than domestic traffic. About 90 per cent of freight traffic is carried by scheduled airlines.

Table 1 shows the regional distribution of traffic. The main shift has been the decline in importance of airlines based in North America and Europe, which in 1988 accounted for about 70 per cent of total traffic (and 85 per cent of domestic traffic), and the rise in importance of airlines based in Asia and the Pacific. Those airlines now account for about 29 per cent of total international traffic and 10 per cent of total domestic traffic. They account for about 20 per cent of all traffic, compared to 14 per cent a decade earlier.

II. THE REGULATORY SYSTEM

Air transport services between cities in any two countries are controlled by an air services agreement (ASA) between the relevant governments. The bilateral strategy was adopted in 1944, following failure to agree on a multilateral exchange of rights of market access. There are now about 1,800 bilateral ASAs.

These agreements usually specify:

- Which airlines will fly on the route;
- The capacity each airline will offer; and

- The amount of capacity that airlines from third countries will be permitted to offer on the route.

The airlines that operate on a route usually include one or more designated airlines from the countries at each end of the route, as well as airlines from third countries. Most of the capacity on the route is provided by the end-point carriers.

Trade in airline services occurs when an airline based in one country sells its services to a resident of another country. A country's imports of air transport services are determined by the provisions of the ASAs. These provisions act like "import quotas" which are allocated to specific foreign firms. The use of country-specific quotas for each "product" (in this case, each route) is similar to the provisions of the Multifibre Arrangement (MFA). A point of difference to the textile and clothing trades is that within one market (i.e. a route), a country will tend to be both an importer and an exporter of air transport services.

In virtually all countries, foreign-owned or foreign controlled airlines are not permitted to provide services between two points within one country (so-called cabotage rights). Domestic markets are regulated in a variety of ways, one extreme version of which is the deregulated system of the United States. However, the United States also denies foreign airlines rights of cabotage.

Fares on international routes are ultimately subject to government control. Traditionally, target fares were negotiated by the airlines themselves and were then referred to the governments for approval. Increasingly, fares are set in the marketplace, and there is less government involvement. Now, once capacity is fixed, market forces set the levels of fares that will fill the seats. Previous attempts to set fares as well as capacity often required government action to counter market forces. The result was a high level of "discounting" and a huge enforcement problem. The increasing number of airlines in the marketplace and the increasing number of substitute routes (see below) have made control of capacity difficult and control of fares even more so.

Recently, a number of ASEAN airlines announced their interest in joining the International Air Transport Association (IATA). IATA

was an important instrument for reaching agreement on fares in the period in which both fares and capacity were regulated, but this role of IATA has since become less relevant. IATA still organizes conferences to discuss fares but these have much less binding influence over members than previously. Garuda was already a member of IATA, and SIA, MAS and Royal Brunei Airlines as well as Cathay Pacific have recently applied to join as trade-association members without voting rights at the fare-fixing conferences.[1] This group of new applicants is credited with having made a major contribution to breaking down the fare-fixing role of IATA. Their interest in joining now arises from IATA's role in providing technical services and financial clearing-house operations, as well as having their new computerized booking system used by travel agents which are certified by IATA. On the other hand, IATA has also relaxed its rule which required member airlines to use only IATA accredited travel agents. Thai, China Airlines and Air China are now the only major Asian international carriers outside IATA.

Various formulas are used to fix capacity under the ASAs. Some depend on rules based on the traffic loads on a route. In other cases capacity is fixed rigidly in advance and then renegotiated at regular intervals, or capacity is reviewed after an interval at the request of the country that has experienced a decline in capacity share.

The designated airlines are required to have substantial local ownership and control. In many cases, the majority owner is also the national government, and then the typical policy is to designate only that one airline as the international carrier.

A. Why regulate?

An original motivation for the system of bilateral agreements was to prevent any one country from exploiting the market power inherent in its control over landing rights. The argument is still frequently made that, without agreements, one side could regulate unilaterally, for profit or for strategic purposes. It is also argued that if airlines were allowed to operate freely, particular airlines, even without explicit government action, would come to dominate the market. At the time the regulatory

1 *Asian Aviation*, May 1990.

system was set up, this concern was focused on United States airlines, as it still is.

A problem with the current system has been the slow pace at which new suppliers are admitted. New suppliers - unless they have large domestic markets or are important destinations - lack bargaining power. Instead, they have to resort to diverting traffic from other routes to build up market share. This strategy has been applied successfully, in particular, by the ASEAN carriers, but the nature of the regulatory system suggests that the market share of new competitive suppliers is less than it would be without the regulations.

Consumers lose from the regulatory system because of the barriers to trade that it creates. On the supply side too there are losers, notably the competitive suppliers of air transport. We argue below that airlines based in the Asia-Pacific region, for example, are competitive suppliers. Thus, the shift in the structure of the market toward the Asia and Pacific carriers would have been even larger without regulation.

III. DEVELOPMENTS IN THE MARKET

Market developments that will have important implications for the evolution of the regulatory system include:

- The increasing density of traffic, especially in the Pacific, owing to the increase in travel and tourism;
- The increasing number of competitive airlines;
- The use of vertical integration in the tourist industry as a strategy for controlling and monitoring service quality (the same strategy is also relevant for the freight market);
- The increasing role of the computerized reservation system (CRS) as a strategic tool for airlines;
- Airport congestion;
- The development of new twin-engine and four-engine aircraft capable of long-distance flights;

- The increased demand for point-to-point services and the wider options for supplying these services, which have increased the number of international gateways and substitute routes;

- The trend towards privatization; and

- Recognition of the importance of networking and of access to mass markets, which has led to the integration of domestic and international services and the multiple designation of international airlines.

There have also been some developments in systems of regulation which we review in this section. Of particular importance is the proposed formation of a single European market from 1993, and its implications for negotiating access to Europe as well as the side effects of negotiations between the EC bloc and the United States.

A. Market density

Tourism arrivals in the Asia and Pacific region have grown at a fast rate, especially in the past decade. The rate of growth has been much higher than in the rest of the world, and the region's share of world tourism traffic is rising rapidly. In 1970, the Asia and Pacific region accounted for about 3 per cent of total tourist arrivals; by 1985 this share had risen to 11 per cent. It is generally expected that over the next decade tourism in the region will grow at rates 25 to 30 per cent higher than the world average - for example, at 7 per cent a year compared with forecast rates of just over 5 per cent for world traffic. This suggests a strong positive relationship between economic growth and the demand for travel services.

Rapid growth in travel volumes means that routes are generally denser than can support more airlines. There are also more routes on offer. For example, flights to Europe from East Asia are now offered via Hong Kong, Republic of Korea, Japan, and all the countries of ASEAN. This is a dramatic change from the 1940s, when traffic volumes tended to be thin. This growth in traffic, within as well as to and from the Asian region, is a major bargaining point in favour of carriers based in Asia. We discuss its significance again below.

Economic development is also likely to be associated with increasing density on the supply side. In the Pacific region, for example, economic development has produced waves of competitive newcomers that have challenged the position of established suppliers. In the late 1970s, carriers based in the ASEAN countries gained access to routes to Europe by offering competitive stopovers. The market is much more competitive than previously, both within a route and between substitute routes.

B. Vertical integration

The growth in tourist traffic in the Pacific is focusing attention on the organization of the tourism industry and its international linkages. A feature of travel demand is that travellers find themselves buying services in unfamiliar countries, perhaps incurring excessive search costs or paying excessive prices. The value of economizing on time in travel creates a role for the intermediary who can arrange an itinerary and deliver the services promised. Predictability of the type of service to be provided is also a selling point with consumers.

To ensure service quality, many tourism firms have sought ways to monitor and control more effectively the supply of complementary services by other enterprises. An extreme option is ownership of the other firm although foreign ownership of airlines is not permitted in many countries (e.g. United States). Other methods of forming vertical linkages involve holding only partial equity or none at all. So far, this strategy has been a feature of the adjustment of airlines based in industrialized countries to a more competitive environment (e.g. JAL, United Airlines).[2]

The importance of the tourism sector for demand for air travel has meant that airlines have begun to take an interest in these issues. Airlines will tend to initiate some connections between third parties in the tourist industry, especially for the purpose of marketing the services of their computerized reservation systems.

2 *The Economist*, 18 August 1990.

C. Computerized reservation systems

An important technological change has been the development of computerized booking systems and the connection of local systems to existing international systems. The immediate advantage of participation in a CRS is that if a system is accepted by a travel agency, flights of that system's owners will be presented first in response to a query. Thus, the development of local systems is also seen as a defence against reliance on the larger United States and European systems, which could disadvantage local carriers.

A couple of systems are being developed in the region. One system operating in the region is called Fantasia, which is managed by Qantas and linked to the Sabre system of American Airlines. Fantasia is still being developed. The more advanced system is called Abacus which is based in Singapore, and involves Cathay Pacific, SIA, MAS, China Airlines and Philippine Airlines. Abacus is connected to one of the European system called Amadeus and will operate from mid-1991. Thai was considering becoming a founding partner in Abacus as well, but a dispute developed over the location of part of Abacus' operations in Bangkok, and the Thai Cabinet ordered the airline out of the system. Since its withdrawal, Thai is reported to have invested directly in Amadeus as a minor shareholder.

The proliferation of systems and the apparent ease of communication among them suggests, however, that the significance of the particular advantage of a system's owners will decline over time. Indeed, it is in the travel agent's interest to be able to access as wide an information base as possible and not be restricted to any one system. Already, some enterprises in the United States offer a service to agents for searching schedules and itineraries for optimum routings. The strategic importance of presenting unbiased information is also recognized by CRS operators.[3]

Perhaps the longer-term advantages of the CRS will be that they can substitute for equity links in co-ordinating services and generating

3 See, for example, M.D. Hopper, "Rattling SABRE: New ways to Compete on Information", *Harvard Business Review* (May-June 1990), pp. 118-25.

networking advantages. They are able to maintain carrier identity in the home country and avoid complications in negotiating capacity under the national ownership requirements of the ASAs. At the same time, they facilitate the creation of conglomerates of airlines. For example, when an agent requests a routing, a single flight number will be given, but the service will actually be provided by a combination of carriers; this is called code-sharing. If so, competition in the market-place between individual firms will tend to be replaced by competition between systems of firms.

Another development related to the importance of the CRS is that access to a particular market by CRS vendors is being introduced into some negotiations over air services agreements. Alongside talks over frequency and entry points, the United States is reported in recent cases (Thailand, Republic of Korea, the Phillipines, Taiwan and New Zealand) to have sought "fair competition" for United States vendors of CRSs and the elimination of biases in any local systems which promote the flights of its owners.[4] The discriminatory aspects of CRS are attracting the attention of competition policy authorities. The EC has recently passed a regulation against discrimination in favour of the airlines owners of CRSs.[5]

C. Airport congestion

A major issue emerging on the Asia-Pacific region concerns the demands that the rapid growth in traffic will create for airport infrastructure. The level of congestion is forecast to rise in most locations.[6] This will impose costs on the airlines, which will be passed on to travellers, and will act as a brake on traffic growth.

A related issue concerns how the authorities responsible for managing airport space will respond if congestion does increase. A

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4 *Australian Financial Review*, 13 February 1990.

5 See Rodney de C. Grey, "1992, Service Sectors and the Uruguay Round", in *Trade in Services: Sectoral Issues* (United Nations Publication, UNCTAD ITP 26), pp. 407-30; as well as Philippe Brusick, Murray Gibbs and Mina Mashayekhi, "Anti-Competitive Practices in the Service Sector" in *Uruguay Round: Further Papers in Selected Issues* (United Nations Publication, UNCTAD ITP 42), pp. 129-56.

6 See, for example, *New Straits Times*, 3 August 1990.

system of pricing which conveys to each user the congestion costs they are imposing on others is efficient, and there is a variety of ways of implementing such as system. Alternatives which employ administrative methods might also be employed. If so, the issue arises of any biases or discrimination between airlines in the management of such systems. For example, will local airlines or incumbents receive a preference?

Important recent technological changes have also occurred in aircraft operating ranges which are relevant to this issue. The development of twin-engine aircraft that can operate over long ranges has widened the scope for more point-to-point services and reduced the importance of hubbing for thin routes. This strategy has advantages for serving particular tourist markets. It can also help to ease constraints on capacity in airports which currently service as hubs (e.g. Narita) by diverting traffic to other centres (e.g. Fukuoka).

E. Privatization

In a rapidly growing tourist market, the provision of air transport services is a critical link. Some forecasts suggest that traffic will grow faster than capacity and that as a result tourism industry firms (e.g. resort operators) will integrate into airline operations in order to control access to services. The interest of the airlines in building connections with the tourist sector was also noted above. The strategic objectives of both airlines and the tourism industry will contribute to a widening of shareholding in many airlines.

In addition, growth will require the purchase of extra capacity. As a result of technical changes that have cut fuel consumption and as a result of lower fuel prices, the share of capital costs in total operating costs has risen rapidly since the 1970s. Airlines will be reviewing the financing of their acquisition of equipment.

Debt finance, which was favoured by government-flag carriers, tends to place a large demand on earnings and raise debt-to-equity ratios too high. Thus there are strong demands for extra capital injections by current owners or - that failing because of fiscal constraints on governments - a broadening of the capital sources. This matches the interest by other service suppliers in buying into the industry. These

pressures from the marketplace and from within the government-owned companies indicate a rapid extension of the privatization moves that are already under way. In the Asia and Pacific region, airlines which are being privatized include Air New Zealand, Philippine Airlines, SIA, MAS, Australian Airlines and Qantas.

Moves to change the ownership structures are proceeding much faster than moves to alter the regulatory environment. That sequencing is appropriate. In addition to assisting the airline to develop a structure suited to a more competitive environment, it removes an obstacle to regulatory reform. Previously, government ownership, fears that subsidization would lead to "unfair practices," and the perception in some countries that retaliation was required were significant complications in the development of an open trade regime for the industry.

F. Networking and cabotage

Experience in the United States market illustrates the economies of establishing a large feeder network.

- Feeder traffic supports a higher level of traffic in any one local market, increasing a carrier's share of departures and attracting a higher share of local traffic (a carrier with a relatively higher share of departures will have a more than proportionate share of the market);

- By managing the timing of feeder flights, a carrier may be able to support flights that are off-peak in some local market and so achieve higher overall load factors;

- By combining traffic from different origins, airlines may be able to offset variability in demand in any one sector and increase the load factor;

- In a hub-and-spoke system, feeder routes can be combined at the hubs and consolidated onto larger aircraft with lower unit operating costs;

The economies of networking have highlighted several issues, including allocation of capacity on international routes and access to

traffic originating at domestic points (cabotage).[7] Asian carriers have expressed concern about the bargaining power of European compared to Asian airlines, and we review these issues in more detail in a later section.

Negotiation of rights of cabotage could influence the ways in which air transport services are provided. The typical approach is to have limited offshore operations. Purchases of inputs like food and fuel will be made offshore, but the extent of capital or labour movements is limited. A foreign carrier might also set up a system for marketing its services. These activities constitute a commercial presence. The granting of cabotage rights might lead to a larger permanent offshore establishment. In other words, liberalization of trade in domestic services is more likely to lead to so-called "establishment-related trade", rather than cross-border transactions. At present, offshore establishments are often limited by rules on the extent of ownership of domestic airline operations by foreigners. These barriers have contributed to the growth in the number of "strategic alliances" which is discussed in the next section.

Another point about the economics of networking is that they have led to pressures for the removal of the artificial distinctions between domestic and international services. As a result, alongside deregulation of domestic services, there will be a tendency towards multiple designation of international airlines. This seems a possibility in Australia and New Zealand and has recently occurred in Japan and the Republic of Korea.

A related issue is the management of domestic and international systems. Within the ASEAN countries, airlines have provided both domestic and international services under the same banner. In some cases, domestic activities are relatively more heavily regulated, for example, through control of fares. Generally, domestic fares within ASEAN countries are said to be relatively low, compared to those in the rest of the world. If so, the possibility of domestic services being used to cross-subsidize international sales is not an issue. The direction of the transfers, if any, is in the opposite direction.

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7 On networking strategies, see Albert Bressand, "Access to Networks and Services Trade", in UNCTAD, *Trade in Services: Sectoral Issues, op. cit.*, pp. 215-47.

The different commercial environments of domestic and international services have encouraged some ASEAN carriers to pass over the domestic systems to subsidiaries. This has already happened in Indonesia and may occur in Malaysia. Passing the service over to a subsidiary also has the advantage of maintaining a degree of control over the feeder system, while maintaining a more explicit commercial separation.

G. The emergence of the megacarriers and "strategic alliances"

Rapid growth in the travel market, the economies realized by the extension of networks, and the value of vertical linkages involving tourism firms and airlines are likely to lead to the creation of systems of firms in the air transport industry. Services, instead of being assembled by consumers, will be packaged by the consortiums, whose activities can be co-ordinated by means of the CRS.

The develoment of the consortiums may extend further, to the emergence of "global airlines" or "multinational corporations" in the airline industry. At present, this step is restricted by ASA rules on national ownership, but the diminishing role of government ownership will broaden the scope for ownership links.

A recent listing of alliances contained 172 items, of which 82 (48 per cent) involved equity investment.[8] Of the equity investments, 46 (56 per cent) were made since 1985. The equity alliance between SIA, Delta and Swissair is the best example of a global arrangement. It covers the co-ordination of fares, of flight schedules, of staff exchanges and, possibly, joint purchasing. Other alliances, such as that involving British Airways and United, do not involve equity swaps but do involve wide-ranging co-ordination of marketing, schedules and codes. At a lower level, alliances might involve joint marketing on a particular route, rather than across networks. Figure 2 summarizes the alliances in which the ASEAN countries are involved.

8 *Airline Business*, August 1990.

It is possible that the emergence of the megacarriers will be a force toward deregulation of the international air transport system, as the efficiency gains from the organization of travel services on an international basis are found to outweigh those of artifical market segmentation on a national or regional basis. If so, the role of the regulatory system in managing the trade in international air transport services could be supplanted by the megacarriers. The era of the megacarriers could then create a set of new policy issues such as the avoidance of the exploitation of power as a result of mergers or co-ordinated marketing.

H. Policy issues

Many of the original motivations for regulation are no longer relevant. Traffic is denser, and there are now more airlines in the market. There are more gateways and more routes that are close substitutes, at least in the eyes of consumers. The moves toward privatization are diminishing the concern about unfair competition from subsidized airlines. In short, the market has become more competitive.

The interests of the tourist industry are being given more weight in many countries. A regulatory system that inhibits growth of capacity in the import-competing air transport industry is criticized by the tourist (or export) sector, which is a consumer of its services. There may be a perception at a national policy level that at least one locally-owned and protected airline is needed either to promote local tourism when it is flagging, or to obtain some share of the benefits of a tourism boom. Usually, however, more efficient fiscal instruments are available for the latter purpose. Furthermore, this argument is uncomfortably close to the position that the original regulators of international air transport were trying to avoid - the exploitation for national benefit of the market power provided by control over landing rights. But the effect of the emergence of the megacarriers on the competitiveness of the market is an important policy issue that will have to be considered.

Within the ASAs, countries can influence the competitiveness of their local air transport markets unilaterally by:

- Promoting fare discounting - if necessary, with the use of more flexible rules on fare setting;

- Reviewing rules on fixing capacity - for example, moving to review of capacity after the event;
- Leaving open the option of multiple designation of local airlines;
- Permitting foreign entry into domestic markets; and
- Easing the rules on the extent of foreign ownership of designated international carriers.

Some countries are already unilaterally varying the conditions of their ASAs along these lines. Thus, working within the structure of their ASAs, it is possible for countries to change the competitive environment in the air transport market. In relation to two other major issues, however, the scope for unilateral action is limited.

One is whether local carriers have an equal opportunity to pick up traffic in other countries. Examples of this issue and how the existing structure of ASAs may fail to provide such assurances are discussed below in relation to the implications of the creation of a single market in Europe and the side effects of bilateral dealing between the United States and Europe.

Apart from these issues relating to market access, the second area of concern is access to services which are complementary to air transport. The question of the access to CRSs was noted above. In addition, there are concerns that, in an era when traffic is forecast to grow rapidly so that airports will become increasingly congested, rules on access to other services such as landing rights, airport gates, or even baggage handling services, will be applied in a discriminatory fashion. It is the case that, because of technical-capacity constraints, not every country which wishes to use a facility like an airport may be able to do so. In that case, it may appear that access is discriminatory. But this need not be the case if there is equal opportunity to bid for access.[9] We discuss these issues in more detail below.

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9 See R. Snape, "Prospects for Liberalizing Services Trade", in L. Castle and C. Findlay, ed., *Pacific Trade in Services* (Sydney, Allen and Unwin, 1988).

IV. ASEAN COMPETITIVENESS

An indication of the extent of the competitiveness of airlines based in ASEAN is the growth of their international scheduled traffic relative to the rest of the world. Five ASEAN countries are all among the top ten fastest growing suppliers of the service (others are Brazil, India, Korea, Pakistan and Saudi Arabia). Table 2 reports ASEAN countries international tonne kilometres performed over the decade to 1988. It shows that their traffic volume has increased nearly four-fold, while their share of regional traffic has nearly doubled and their share of world traffic has increased by a factor of four. We now examine in more detail the origins of the apparent international competitiveness of the ASEAN carriers.

Some of the factors determining competitiveness depend upon conditions in the home country (wages, for example), others on the technology of airline operation, and others may depend on the interaction of location and regulation. The technology of airlines is such that most countries can supply air transport services, but that there are significant differences in the cost of doing so. The two key determinants of costs are (a) labour conditions and (b) managerial and labour skills.

A. The determinants of airline costs

1. Technology

The technology of air transport production, to a large extent, is embodied in the aircraft which produces them. In addition, the technology of information and telecommunications systems, also embodied in the equipment used, is important. Thus the technology is available to any country or any airline, though the extent to which airlines use the most recent technology depends on their own strategic choices. There may be constraints, for example, on the ability of an airline's labour force to use the available technology effectively. In short, lack of appropriate technology is not a factor which limits a country's entry into trade in airline services.

2. Finance

Few countries face serious problems financing entry into the industry, though countries which have serious debt problems may face difficulties in raising new capital at the lowest interest rates. While the amount of funds required for new aircraft are large, it is not the case that the industry is capital-intensive. Capacity-related costs are a relatively small proportion of total costs. The conditions under which airlines are able to obtain finance do not differ much from country to country. Indeed, some of the less profitable United States airlines may have greater problems in raising finance than successful airlines in developing countries. Leasing aircraft is an option which many airlines are adopting, partly as a response to financial limits being imposed on government-owned airlines.

3. Fuel

Fuel is an important input, but it is not a source of differences in cost in providing services. All airlines flying between London and Singapore, for example, and fuelling in those cities, will pay much the same price for fuel. Fuel prices vary from region to region, and from city to city, however. Access to specialist maintenance services is open to all airlines at similar prices, though airlines based in the United States and Europe have the advantage of greater proximity to, and choice of, supply.

4. Labour

Of all inputs, labour is the most significant in the production of airline services. Labour can account for up to 50 per cent of an airline's total costs. Apart from directly employing labour, airlines purchase a wide variety of goods and services, such as advertising, food and computing services, all of which have a high labour content. The prices of goods and services, such as might be used as inputs into production of airline services, are highly correlated with the price of labour, both

across countries and over time. Thus, the price of labour is the single most important determinant of input prices which airlines face.

Airlines employ labour of very different skill levels. Pilots are highly skilled, and there is an international market for pilot services (though there is still a correlation between average pilots' pay and their base country's per capita income). Many pilots employed by an airline of one country may come from other countries, especially in the case of airlines of developing countries. Pilots account for only a small proportion of an airlines total costs, however. A large proportion of an airlines expenditure on labour is accounted for by the skilled and semi-skilled categories, such as maintenance workers and flight attendants. These employees tend to be nationals, and their pay reflects national pay rates. The same is true of unskilled employees. It is difficult, when making cross-country comparisons, to obtain an accurate measure of labour input, since the unskilled labour employed in low-income countries may be less productive because of lower skill levels, for example. In these circumstances, the wage paid is not a good indicator of per-unit labour costs.

An important trend in the industry is towards international sourcing, especially of labour. Airlines have always purchased some inputs internationally, but usually this has been where they have had to do so (e.g. in purchasing handling facilities at destination countries). There is scope for airlines to rely more on inputs purchased from abroad, especially when home costs are high. Thus, airlines of high cost countries can hire labour (e.g. flight attendants), undertake more maintenance, and undertake information processing away from the home country. They may do this to remain internationally competitive. This has implications for ASEAN airlines. Competitors may be able to lessen the ASEAN airline's competitive edge, but the ASEAN countries themselves may also develop export markets in airline inputs - such as aircraft maintenance.

Analysis of airline cost data suggests that a combination of low wages but high skill levels creates favourable conditions for a highly competitive airline.[10] In the early stages of industrialization, growth in skill levels and labour productivity can outpace growth in real wages.

10 Christopher Findlay and Peter Forsyth, "Competitiveness in Internationally Traded

As a result, a number of rapidly industrializing countries in Asia and the Pacific found themselves in this position. This put them in a very different position to other slower-growing developing economies. It need not be the case that developing and newly industrializing economies (NIEs) are uncompetitive in this industry. Nor need it be the case that these countries' airlines depend on the regulatory system for their survival. On the contrary, our argument is that the current regulatory system inhibits their growth. A side effect of rapid economic growth is that the volume of traffic also increases, both inbound and outbound tourist and business traffic, as well as freight. This growth in the size of the market has the benefit of increasing the barganing power of NIEs in the negotiating process.

5. Management

A final input, which is impossible to measure or price, but which is very important, is that of management. In some low-income countries, managerial skills may be in short supply. Managers can, to an extent, be purchased on an international market. Management can make a major difference to the efficiency with which an airline turns inputs into output.

Costs depend not only on the prices paid for inputs, but also on how efficiently inputs are converted into outputs. In the case of airlines, it appears that not only is access to good managerial resources important, but also the gains from "learning by doing" are substantial. As a result, while airlines of the advanced industrial countries have been the more efficient, the airlines of the NIEs, and the ASEAN nations in particular, have been catching up on them. This growth in productivity combined with relatively low input prices, gives them a cost advantage.

Services: The Case of International Airlines; *ASEAN-Australia Working Paper*, No. 10 (Kuala Lumpur and Canberra, ASEAN-Australia Joint Research Project, 1984).

6. Service quality

Passengers do not necessarily prefer to fly on the airline which offers service between A and B at the lowest price. A number of other aspects are important. One of these is quality of service, a "catch-all" term which can refer to in-flight service, baggage handling reliability, on-time performance, booking convenience, as well as the perception of safety. Quality is not easily measured, though surveys of "most preferred airlines" give an indication of quality and most ASEAN airlines have good reputations for service quality. Quality can be increased by better management and more inputs. Some airlines, such as SAS, incur high costs but provide high quality services.

7. Scale

By and large, scale does not affect the costs with which an airline can produce a service - a small airline can be a cost-effective airline, as can a large airline. Scale is more important on the marketing side. A large airline may find it easier to develop an attractive network, and offer frequent services, than a small one. It will also be able to make the large up-front investment in a CRS, since it will have access to the capital required, and it will be able to use the system effectively itself.

8. Contracting out

There is a growing distinction between airline operation and air services marketing. Most airlines actually operate their own services and market them as well. This need not be the case, however. It is possible for one airline to operate the services, and another to market them. This could come about through one airline "contracting out" operations to another. While this does not happen on a large scale, it happens frequently, and there is scope for it to happen at a large scale. The significance of this is that even if airlines may lose out at the marketing end, they may not lose out at the operational end. Thus, a small airline with a poor network - but which has low costs - may not be supplanted by a larger one with better networks but higher costs: it may

contract to provide services for the larger airline. This has significance for the ASEAN airlines which may have low costs, but in a particular area little market access, whereas airlines of the industrial nations have market access but high costs. Ultimately, what happens depends on whether these airlines are willing to contract out services. Cost pressures could force them to do so.

9. Regulation and competitiveness

The regulatory system can have an indirect effect on competitiveness through the constraints it imposes on the building up of a network. We argued above that there were economies in the structure and size of networks. Access to landing rights depends on negotiating strength in the present system. Negotiating strength depends on a combination of location and market size (both origin and destination traffic). In principle, in the present system, a country may be a highly competitive supplier of air transport services but be unable to exploit that competitiveness because the negotiating process has restricted its networking options. The ASEAN countries, however, have been able to exploit their location and will increasingly be able to use growth in the demand for travel to and from ASEAN in the bargaining for traffic rights. In the next section, we review some empirical work in the measurement of relative competitiveness of particular airlines.

B. Airline competitiveness: present patterns

In analysing the patterns and trends of airline costs, it is only possible to draw upon a small group of studies which were undertaken for differing purposes. Data and time limitations prevent a systematic investigation of the issue. Nevertheless, it is possible to draw some clear lessons from the available data.

Information on the input prices facing airlines of different regions in 1983 is presented in tables 3 and 4. It is clear from table 3 that Singapore Airlines had distinctly lower costs than all other airlines in the sample. The highest costs were faced by the Japanese and United States airlines (the value of dollar high at the time).

In table 4, data are presented for four groups of airlines: (i) those from ASEAN countries; (ii) airlines of Pacific-rim industrial countries, (iii) airlines from poor populous Asian countries, and (iv) two airlines from Europe. The picture is much the same as that shown by table 3. The ASEAN airlines face low input prices relative to those of the Pacific-rim industrial countries and the European countries, but they face higher input prices than the Indian and Pakistani airlines.

Input prices and productivity determine output prices. Evidence on cost per unit of output is presented in table 4. Since costs depend on stage length, aircraft size and load factor, an adjusted measure of output which standardizes for these variables is used. It is unwise to read too much into the estimates for any one airline, but the broad pattern is probably reliable. It appears that the ASEAN airlines are able to achieve costs which are as low as any others. They are matched (in 1983) by costs of the Indian and Pakistani airlines, on the one hand, and by the North American airlines on the other. In productivity terms, the North American airlines are the best performers (also reflected in table 3) and the ASEAN airlines are middle level performers (at the level of European airlines, such as British Airways). No allowance is made for service quality in these data. Clearly the apparently poor performance of SAS could be attributed to high quality. However, the ASEAN airlines' good cost performance and moderate productivity is unlikely to be at the expense of quality.

As of the mid 1980s, the ASEAN countries' airlines were competitive. However, over time, there are some forces which operate in the direction of making them more competitive, and others making them less competitive. Some of these forces are quite systematic, while others are random. We turn to the examination of trends in the competitiveness of these airlines.

D. Airline competitiveness: future trends

An important element among the key factors that determine the competitiveness of an airline is the rate of growth of real GDP per capita (or real productivity per employee) in the home country. The rate of growth of real wages is likely to approximate this variable in the long term. It need not be the case for the short to medium term (say,

within a decade) that the two correspond. For example, real wages may be held down while the economy grows quite rapidly. However, eventually real GDP per capita growth leads to real wage growth. This in turn leads to growth in real airline wages. Again, it need not always be the case that airline and non-airline wages will move at evenly the same rate. For example, labour market regulations may impose constraints on particular wage categories. However, the two will tend to move together. Thus, airlines based in countries with relatively high growth rates of GDP per capita will experience input prices rising more rapidly than input prices of other airlines, and, other things equal, will lose their competitive advantage. The high GDP per capita growth rates of the ASEAN countries makes them less competitive over time.

The pattern is complicated by inflation and exchange rate movements. If inflation rates are high, input prices will rise. However, exchange rates will tend to depreciate in high-inflation countries (and rise in low-inflation countries) so as to preserve the country's real trading position. Thus, inflation as such will not weaken the airline's competitiveness in the medium to long term. Real exchange rates can change, however. For example, a country might experience a petroleum export boom, which will push up real exchange rates, and make existing tradable industries, including airlines, less competitive. Alternatively, worsening terms of trade for traditional exports will enhance the competitiveness of a country's airlines. These changes have affected ASEAN countries in the past, and can be expected to do so in the future. However, they are not predictable or systematic, and it is not possible to identify any trend. The main systematic determinant of relative input prices is the growth of GDP per capita.

There may also be changes in efficiency, as measured by total factor productivity. These changes reflect either improvements in technology, making even the most efficient producers more efficient, or a catch-up of the less efficient producers so as to more closely match the performance of the most efficient. It is clear that the competitiveness of the ASEAN airlines will depend on their relative productivity growth, and since, as of the mid 1980s, they were not in the most efficient group, there is scope for relatively rapid growth in productivity.

These forces in the determining of costs are examined in table 5. Data limitations prevent a large sample from being assembled, but airlines in each of the four groups of interest are represented in the table. Growth in real GDP per capita, 1978 to 1988, is reported in the first column. It is clear that the ASEAN nations had much higher growth rates than all countries except Japan. Other things equal, this would have weakened their competitive position. It is possible that the higher relative GDP per capita and real wages could also have been accompanied by greater labour and management skills, leading to efficiency improvements in airlines. However, it is not feasible to check this hypothesis.

Another factor which will affect the competitive positions is the movement in real exchange rates. Price increases 1988 over 1978, compared to the price increase in the United States are reported in column 3. Malaysia had a higher inflation rate than the United States, whereas Singapore had a lower inflation rate. However, over the period, the Singapore dollar appreciated relative to the United States dollar, while the Malaysian currency depreciated. Since the increase on the general price level in Singapore was small, the overall result was that the Singapore dollar, in real terms, depreciated relative to the United States dollar, while the Malaysian currency rose (column 4). Over the period, the real exchange rates of the United Kingdom and Japan, along with Malaysia, rose significantly, while the exchange rates of India, Pakistan, and to a lesser extent, Australia, fell (relative to the United States dollar).

Putting the changes summarized in columns 1 and 4 together yields column 5 which is the change in real GDP per capita expressed in United States dollars. In column 6, this is expressed relative to the United States change. These columns provide an indication of the patterns of change in the main determinant of airline input costs over the period. The movements in actual airline input price indexes would be less sharp than these, since labour prices, and prices which depend on labour prices, do not account for all airline costs. Nevertheless, the two columns will indicate how the different airlines are affected by input price changes.

These tables highlight the difficulties that have been overcome by the ASEAN airlines. Of the sample, only JAL, facing high real wage

growth and a rising yen, has faced a more difficult environment. Singapore's high real wage growth, and Malaysia's appreciation, have made it difficult for those countries' carriers. In short, because of high growth at home, the competitiveness of the ASEAN airlines has lessened in the 1980s, and this process is very likely to continue.

This trend in input prices has been offset by greater productivity growth. In the late 1970s, the ASEAN airlines were less productive than airlines of OECD countries, but they were able to more than compensate for rising costs by improving productivity. In column 7, cost per available tonne kilometre, in United States dollars in 1988 is compared to that in 1978, and in column 8, the movement relative to that for the United States airline, Pan Am, is reported. In fact, the very small measured change in SIA's unit costs may not be a reliable measure of actual unit costs. Over the period, the airline specialized more on longer haul routes. Average stage length increased by nearly 60 per cent. Longer routes are cheaper, per kilometre, to operate, and therefore the fall in output costs relative to input costs may not be due entirely to productivity improvements. Nevertheless, it is clear that the ASEAN airlines have been more than making up for input price increases by productivity growth. This is consistent with the results in table 3, and Brunker, Findlay and Forsyth report that over the period 1975-83 the airlines of the NIEs economies experienced twice the productivity growth of airlines of North America, the rest of the industrialised countries, and the developing economies.[11]

High productivity growth can continue while an airlines' productivity levels are lower than those which can be achieved by the most efficient airlines. Once this level is reached, productivity growth is constrained by the pace of technological improvement. As of 1983, the ASEAN airlines still had some way to go to the frontier, but over the rest of the 1980s, they would have closed the gap. While there is still probably a gap between SIA and the most efficient North American and Japanese airlines, SIA is now probably one of the most efficient outside these groups.

11 D. Brunker, C. Findlay, and P. Forsyth, "Comparative Advantage in Airline Services", Paper presented to the Economists' Conference, Adeleide, July 1989.

The various opposing forces can be summarized as follows. The ASEAN countries' airlines are amongst the world's most cost-competitive. They can continue to stay this way, and they may improve their position over the next decade. They will face more rapidly rising input prices than airlines of other groups, such as the airlines of the industrialized nations, because of the success of their home economies. Nevertheless, it will be possible for them to counter and outweigh this disadvantage by achieving, as they did in the 1980s, higher productivity growth.

V. LOCATION AND COMPETITIVENESS

Airline markets have a locational dimension, and the location of an airline's home base can be an important factor in determining how effectively it can compete in particular markets. Arguably, an airline is most competitive in the region around its home base, since it has greatest control over its operations and marketing there. In addition, airlines which have relatively low costs, as the ASEAN airlines, will find that in other regions, they will face higher input costs. Thus, the cost of tasks performed in Europe for an ASEAN airline (baggage handling, advertising) will reflect European, not ASEAN, wage levels.

It is worth identifying a number of distinct markets, and discussing them separately. Those examined are; (a) the intra-Asian market: (b) the trans-Pacific market, and (c) the Asian-Europe market. We also discuss the intra-Europe market in more detail in the next section. While there are other markets in the world, e.g. the North Atlantic, it is assumed that these are of limited interest to the ASEAN airlines.

A. The Intra-Asia market

In this market, the ASEAN airlines can be expected to be in a strong, though not dominant, position. They will be sharing the market with airlines of other NIEs (e.g. Cathay Pacific from Hong Kong), which face similar input costs, similar trends in input costs, and which are similarly efficient. There will also be some participation by the smaller airlines in the region. The ASEAN airlines will have a distinct cost advantage in routes to/from Japan over Japanese airlines, but the

extent to which they are able to take advantage of this depends on the regulatory framework on these routes, which could continue to be quite restrictive. The location of the ASEAN countries is such as to provide them with quite well-located levels, especially in comparison to airlines based on the fringes of Asia (e.g. Korean Air).

B. The trans-Pacific market

The ASEAN airlines' location is not as convenient for trans-Pacific routes, mainly to the United States and Canada. It is not a major problem: access to markets is perhaps more of a problem. ASEAN costs are likely to be the lowest of those airlines actively participating in that market. What the North American airlines lose on input costs, they make up in terms of efficiency. ASEAN carriers have a considerable cost advantage over the Japanese airlines, however.

C. The Asia-Europe market

In this market the ASEAN airlines have a distinct advantage. They have lower costs than the airlines of industrial countries on the fringe of Asia (Japan, Australia), and significantly lower costs than the European airlines. They and the airlines of other NIEs will share the market with smaller Asian airlines, but they are likely to be the dominant carriers. The European airlines will continue to serve Asian routes, but their share of markets will depend on regulatory factors. If markets are relatively liberal, it is likely that the ASEAN airlines will gain market share at the expense of the European airlines. It is also quite possible that the interest of the latter in serving Asian markets may diminish. While the Asia-Pacific is the most rapidly growing market in the world, it is possible that the Eastern Europe market will also be growing rapidly, and the European airlines could concentrate their efforts for the next decade on that market.

VI. A UNIFIED EC MARKET

As from 1993, the EC will be regarded as a unified air transport market. This change was prompted by a court decision that air transport should be subject to EC competition rules. The bilateral ASAs

were not consistent with those rules. The effect could be to create conditions of free entry into EC routes for any EC carrier. These changes have a number of implications which we now examine, drawing upon the analysis of costs and competitiveness.[12]

There is a variety of degrees of efficiency and competitiveness amongst the European carriers. Free entry and a competitive market within the EC could lead to pressure for significant changes, as occurred following deregulation within the United States market. One difference in the European case is that a significant number of airlines are owned by governments. This will restrict the number of mergers or takeovers which are possible in the short run. The immediate adjustments are therefore more likely to involve changes to networks and differential rates of growth according to competitiveness. A side effect, therefore, of more competitive conditions in the home market, and the adjustments to raise efficiency and to minimize costs, could be an increase in the degree of competitiveness of EC carriers outside Europe.

Airlines of countries outside the EC also now operate on intra-EC routes. It is expected that, as a result of the declaration of a unified market, these routes will be declared "domestic". Airlines from outside the EC operating on these routes would then have rights of cabotage. Normally, as noted above, cabotage rights are not extended to foreign carriers. In this case, it is reported that the EC Commission's expectation is that the EC will continue to honour existing bilateral grants of such rights.[13] As a result, foreign carriers who now operate on intra-EC routes are unlikely to be denied access. It will, however, be much more difficult to gain rights of access to intra-EC routes after 1993.

Some countries might respond to constraints on future growth of intra-EC traffic rights by trying to restrict the traffic rights of EC carriers in their own region. Few countries have the bargaining power to retaliate effectively in this way. One country that could do so is the United States. The United States has already threatened to deny EC carriers access to intra-US routes. The outcome of this strategy could

12 See also Grey, *op. cit.*

13 J.W. Young, "What will be the Effects of EC Unification on International Air Services After 1992?", *ICAO Journal*, Vol. 45, No. 1 (January 1990), pp. 25-8.

be bilateral exchanges of cabotage rights between the United States and the EC.[14]

If this exchange of cabotage rights did occur, then (as our analysis of the gains from efficient networking indicates) the competitiveness of both EC and United States carriers outside either region could be enhanced. This is another indirect effect of the creation of a unified EC market.

One qualification to this point, which is also relevant to Asian carriers concerned about developments in the EC, is that the extent to which United States carriers take up more ports in the EC may be limited. There are two reasons. First, the economics of long-distance transport favour the use of very large aircraft and the operation of a hub-to-hub service. Collection of traffic at either end of a route is often more efficiently performed by feeder services to the hub rather than by the use of "dog legs" with the larger aircraft. The creation of a feeder system would be relatively more costly for a carrier based outside the region than for one based within. The second factor is that there is already substantial congestion at the major airports in Europe. This will limit the extent to which new intra-EC networks can be established.

From the point of view of countries other than the United States, a major concern is that in future the EC may negotiate its ASAs as a bloc. At this stage, it is not clear how these negotiations will proceed. It is possible that ASAs will still be negotiated bilaterally by individual EC countries. If the EC did negotiate as a bloc, it need not diminish the bargaining power of the other country. The reason is that the basis of the bargain becomes the total traffic between that country and the EC. Either party has an equal claim on rights to carry that traffic.

The more important issues, other than shares of capacity to and from Europe, could be the rights of access to intra-EC traffic. However, for the same reasons noted above, the construction of an elaborate intra-EC network may not be profitable from the point of view of airlines, like those in ASEAN, based far away.

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14 This strategy is discussed in more detail by D.M. Kasper, "Liberalizing Airline Services: How to Get From Here to There", *World Economy*, 11 (March 1988), pp. 91-107.

The most important issue may be the procedure of allocating landing rights at the congested airports. The creation of a unified market could lead to an overall higher level of priority for EC carriers for access to services. Even though individual countries outside the EC may be able to negotiate substantial capacity to and from Europe, they may not be able to use their preferred airports in the EC, if other EC carriers have first choice.

One response to the constraints on developing routes within the EC could be for carriers such as those in ASEAN, to extend and consolidate their strategic marketing alliances with EC carriers. In that case, for example, the EC carriers could provide feeder services in Europe to the ASEAN carriers' entry points. The ASEAN carriers would then provide the long-distance haul and the regional network in Asia. The construction of this sort of marketing alliance could also facilitate ASEAN carrier access to preferred airports in Europe. Some ASEAN carriers already have established these sorts of alliances (see figure 2). Others are yet to formalize such relationships.

Another strategy for handling some of the issues which are highlighted by EC market unification is to draw upon bargaining powers beyond the current institutional arrangements for trade in air transport services by employing the principles and procedures considered for the multilateral framework for trade in services being negotiated in the Uruguay Round. We review these points in the next section.

VII. PRINCIPLES OF THE MULTILATERAL FRAMEWORK

Negotiations are currently underway on a multilateral framework for trade in services based on a set of principles agreed up on the Mid-term Review of the Uruguay Round held in Montreal in December 1988. In this section, we review the "Montreal" principles and their treatment under the system of ASAs.[15] We establish that important principles, such as most-favoured-nation (MFN) treatment and national treatment, are violated by the current system of bilateral agree-

15 See also Christopher Findlay, "Air Transport", in P.A. Messlin and K.P. Sauvant, ed., *The Uruguay Round: Services in the World Economy* (Washington, D.C. and New York, World Bank and UNCTC, 1990).

ments. We then note the relevance of those principles for handling some of the issues that arise out of developments in air transport markets.

A. Market access

Do suppliers have the opportunity to sell the service in a foreign market? When applied to trade in services, the market access concept, to which this question refers, includes all forms of trade, both establishment and across-the-border.

In the case of air transport, market access is limited by the bilateral agreements. The ASAs specify both the markets (routes) which can be served and the traffic which can be carried. In some instances, as when foreign suppliers try to enter route in a domestic network of another country, market access is denied. In addition, there are usually limitations on the form in which an airline can export its services because of the rules on foreign ownership.

B. Transparency

While all ASAs are registered with the industry body, the International Civil Aviation Organisation (ICAO), the published agreements contain the general rules on setting capacity and so on. There are often side agreements which are not published and which contain details on rules used for setting capacity, for example. The ASA system would only be transparent if all such agreements are published.

C. Most favoured nation

The MFN principle is a tool designed to avoid discrimination between foreign suppliers in any market. Its implication is that, having established the conditions for market access, there should be no discrimination between potential foreign suppliers.

This principle is violated by the ASAs. Market access rights are exchanged bilaterally and on a reciprocal basis. The system is based on the balancing of benefits between pairs of countries. As a result, the ASAs are highly disciminatory. For example, there are more severe

restrictions on market access for airlines from third countries than those at the other end of the route.

It was noted above that the degree of discrimination is subject to the bargaining powers of the parties involved. Developing countries which have a small domestic traffic flow, or which generate few international passengers, either as an origin or as a destination of traffic, tend to have little bargaining power in the international negotiations over the conditions of the ASAs. These differences in the degree of bargaining power are likely to be exaggerated by the formation of a common European market, and the bilateral dealing that may follow between the EC and the United States.

D. National treatment

If the principle of national treatment were applied to air transport, it would mean that foreign airlines would receive no less favourable treatment in any market than would domestic airlines, in terms of all rules, regulations, and administrative practices.

This principle is not applied in the ASAs. The restrictions on acces to domestic routes is one example. Other issues include the common rule that government officials must fly with a national airline. As noted above, issues are emerging in relation to access to business practices and complementary services, such as access to ground-handling services, landing rights and fees, and financial aspects such as the remission of profits. The two key issues in this area noted above were access to computerized reservation systems and the administrative practices adopted to allocate airport space in an increasingly congested environment.

VIII. CONCLUSION

The principles on which the Air Service Agreements (ASAs) which govern international trade in air tranport services are based are entirely different to those agreed upon as Montreal. The ASAs stress reciprocal benefits, while the Montreal text stresses MFN. The ASAs and associated regulations put up barriers between domestic and international markets, while the Montreal text stresses national treatment.

These differences mean that the application of the basic principles of the Uruguay Round multilateral framework for trade in services to the trade in air transport services would unravel the existing regulatory structure.

The dilemma is that because of developments in the market place, a number of countries will find that the ASA approach will not help solve their market access problems. There are three important instances where these market access issues are likely to be exaggerated in future. These are:

- The side effects of bilateral dealing between a unified European market and the United States, involving the exchange of cabotage rights;
- The growth in importance of computerized reservation systems and the biases in market access that those systems, at least in the short run, will involve; and
- Discrimination in access to other services complementary to air transport, especially those related to airports.

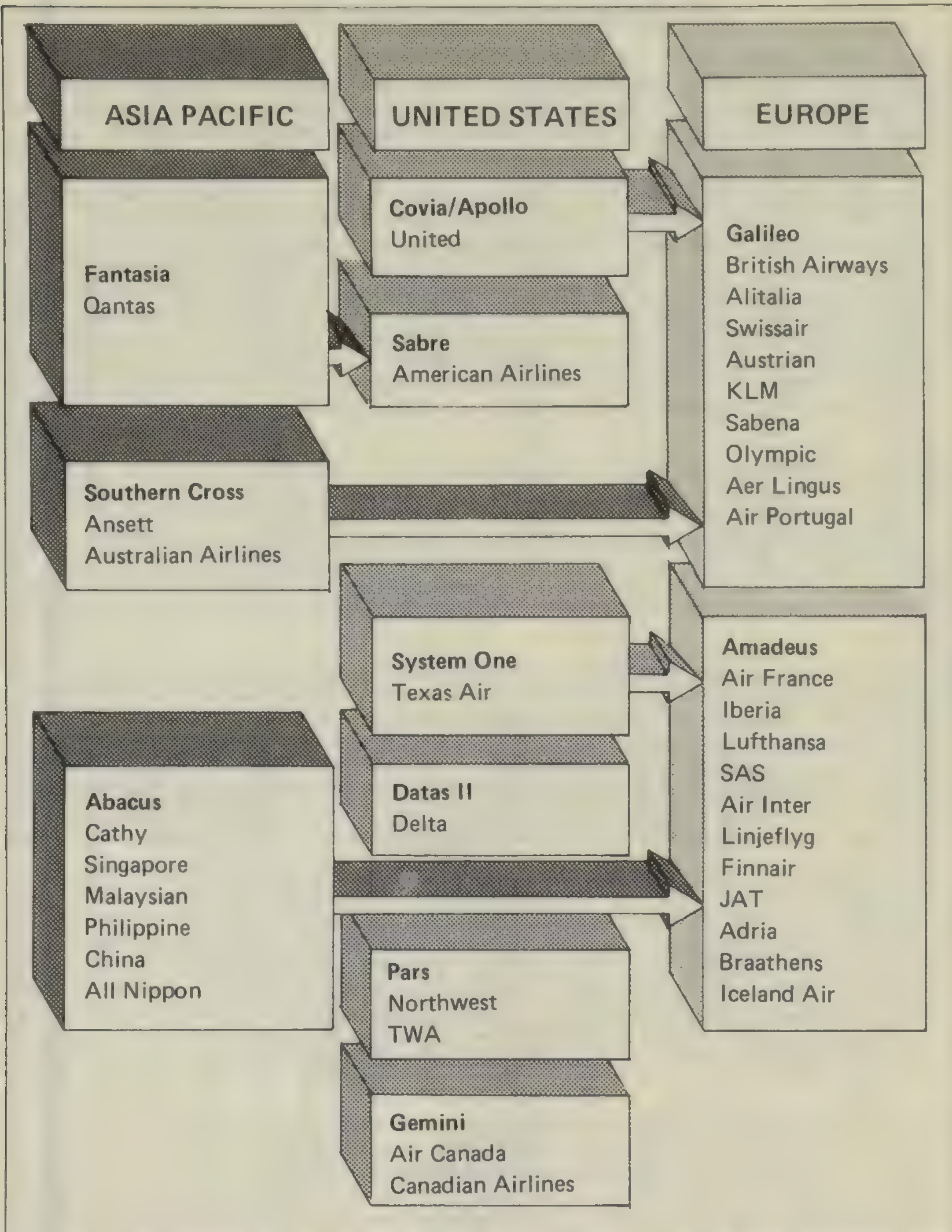
Of these three sets of issues, our analysis suggests that the third is the most important. The indirect effects of EC/United States bilateral bargaining may not be significant, because its impact on the networks of United States or EC carriers within either market is likely to be small. The direct implications, possibly of having to bargain with a united Europe, are offset by the growing bargaining power of the ASEAN airlines, because of the rapid traffic growth in the region. If there were some concern about negotiating strengths, the ASEAN carriers could meet to co-ordinate their positions. The second issue, of possible biases involved in CRS, are likely to be mitigated by further technological changes and the commercial incentives of the CRS owners and operators.

Some developing countries argue for continuing the current arrangements on the grounds of the need to develop their national airlines. Our analysis of the sources of competitiveness in this service suggest that many such countries will already be highly competitive. This argument certainly applies to the ASEAN countries. The evidence is that developing-country suppliers have been able to penetrate world

markets, although to a lower degree than might otherwise have been observed because of the restrictive effects of the ASAs. Again, the ASEAN experience is a dramatic illustration of this point. These results weaken the argument that the important benefit of regulation is to give protection to developing-country airlines in order to promote their development. Those airlines are, on the contrary, hindered, not helped, by the current arrangements.

Whatever the benefits perceived in the current arrangements from a developing-country perspective, their continued use will involve the cost that they will not help in promoting the market access of their airlines. A choice will have to be made on the trade-off between continuing with the familiar system, based on specific recoprocity, compared to a shift towards a new set of principles, namely a greater degree of market access through the application of the multilateral framework of a more diffuse exchange of traffic rights.

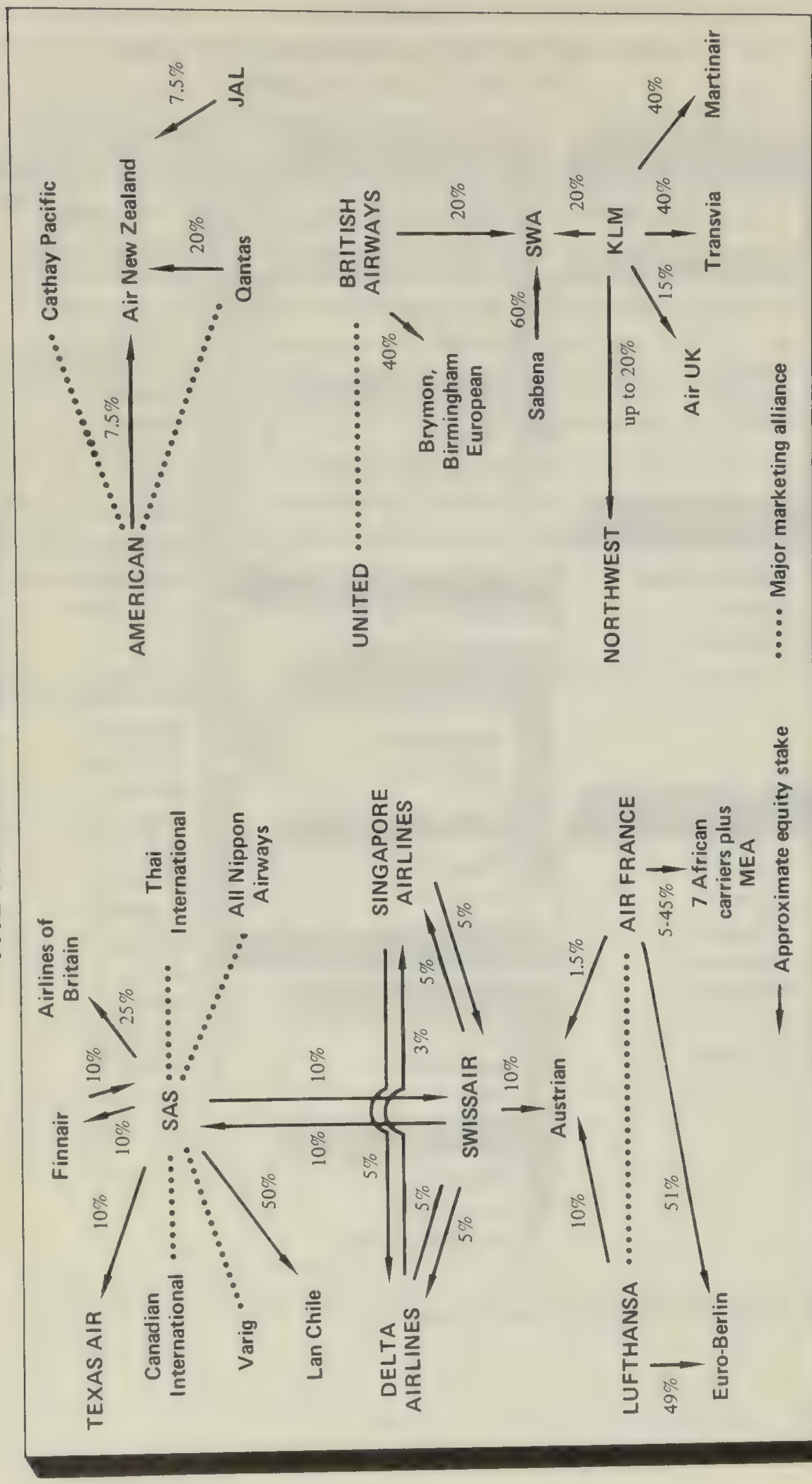
Figure 1
AIRLINE COMPUTER BOOKING SYSTEMS: THE STATE OF THE GAME



Source: Sydney Morning Herald, July 11 1989.

Figure 2

THE AIRLINE FAMILY TREE



Source: Avmark Aviation Economist and Far Eastern Economic Review, 15, February, 1990, p.37

Box 1

AIR TRANSPORT IN THE URUGUAY ROUND

Unlike in most other service sectors, trade in air transport services has been covered by a multilateral convention (Chicago Convention) since 1944, administered by the International Civil Aviation Organization (ICAO) and by a complex web of bilateral air service agreements (ASAs). [a]

Market access is basically obtained in the exchange of bilateral landing rights, including in some cases "fifth freedom" rights. However, cabotage is almost universally reserved for national carriers. Bilateral greements specify national treatment to be otherwise accorded to each designated airline. Multilaterally, in the Chicago Convention, article 15 (airport and other charges) and article 9 (prohibited areas) are also based on national treatment. Competition among scheduled services takes place on the basis of quality services (higher value-added), including through networking rather than price. Strict application of an unconditional most-favoured-nation clause would be the antithesis of the existing system. In common parlance, a distinction is drawn between the bilaterally negotiated ASAs described as "hard rights", and "soft" rights related to ancillary services such as computer reservation systems, landing rights, etc.

Ironically, while initiatives to set up a multilateral regime in 1944 were opposed by countries fearing dominance by United States carriers, the United States Government is now under strong pressure from its domestic industry to exclude the air transport sector from the multilateral framework for trade in services. The immense size of the United States market and its variety of destinations make it difficult for the United States to find sufficient motivation to negotiate increased access commitments, even on a bilateral basis, with smaller countries with limited destinations, small domestic markets and physical constraints to increasing the number of flights.

Many developing countries, including some within the Asia-Pacific region, have felt that the current bilateral structure has served them well. Others, particularly Singapore, have favoured a more multilateral approach. [b] The ICAO Council has addressed, in October 1989, the GNS negotiations, and based on its resolution A27-14, the Council of ICAO issued a statement to the GNS on 25 April 1990, which noted that "for developing States the bilateral process allowed to negotiate access to developed country markets on a reciprocal basis, thus greatly increasing their participation in this sector". Also it was mentioned that the bilateral approach had enabled liberalization "at a pace determined by partner States' mutual desire for change".

As in other service sectors, Europe 1992 arises as an element in the negotiations, as the eventual implications for the existing structure of agreements of the adoption of a Common Aviation Policy in the EC are still not clear, which could involve the EC as a unit renegotiating all the member States' ASAs with third countries. However, no participant in the Uruguay Round appears to be pressing for a dismantling of the current system at the present time, and attempts are being made to qualify the MFN clause in such a way as to permit the air transport sector to be "covered" by the multilateral framework. The question arises as to whether, within such a framework, some access commitments with respect to "hard" rights (e.g. fifth freedom rights) could be negotiated and included in schedules in exchange for concessions in other service sectors.

In the view of most participants, there are many possibilities to apply the basic principles of the multilateral framework (e.g. progressive liberalization, increased participation of developing countries) to a variety of ancillary services including ensuring non-discriminatory access to computer reservation services, overcoming discrimination in ground-handling facilities, repair and maintenance, etc. The European Community has proposed a sectoral annotation which would apply the principles of the framework to such services.

a The details have been described by Findlay and Forsyth in their contribution to this volume.

b See "L'avenir du transport aérien mondial se joue en Europe", *Le Lloyd Anversois*, 5 September 1990, pp. 1-3.

Table 1

REGIONAL DISTRIBUTION OF SCHEDULED AIR TRAFFIC, 1988 AND 1979
(Percentage of total tonne-kms performed by airlines registered in each region)

Region	All services 1988	All services 1979	International 1988	International 1979	Domestic 1988	Domestic 1979
North America (Canada and United States only)	39.3	41.5	21.5	21.2	59.5	59.8
Europe	31.0	34.0	35.5	40.9	25.8	27.5
Asia and Pacific	19.9	14.0	28.9	21.4	9.6	7.4
Latin American and Caribbean	4.6	5.0	5.7	6.7	3.5	3.5
Middle East	3.0	3.0	5.0	5.5	0.8	0.8
Africa	2.2	2.5	3.4	4.3	0.8	1.0
ICAO World	100	100	100	100	100	100

Source: ICAO, *Civil Aviation Statistics of the World 1988* (Montreal, ICAO, 1989).

Table 2

GROWTH OF ASEAN CARRIERS IN INTERNATIONAL PERSPECTIVE

Country	*International Tonne-Kilometres Performed (millions)* 1978	1988
Brunei	-	333
Indonesia	198	1,827
Malaysia	276	1,027
Philippines	393	1,127
Singapore	1,355	4,139
Thailand	500	2,030
ASEAN Total traffic	2,722	10,483
Share of Asia + Pacific traffic	18%	32%
Share of world traffic	2%	9%

Source: ICAO, *Civil Aviation Statistics of the World 1978, 1988* (Montreal, ICAO, 1979, 1989).

Table 3

INPUT PRICES AND TOTAL FACTOR PRODUCTIVITY, 1979-1983

Airline	*Input price index, 1983 (BA = 100)*	*Total factor productivity index (inverse) (BA, 1983 = 100)*			
		1979	*1980*	*1983*	*1984*
SIA	94	120	111	98	92
Qantas	120	103	101	96	-
Canadian International	116	72	69	68	62
JAL	127	92	83	79	75
Pan Am	136	76	79	76	78
SAS	114	85	85	91	97
BA	100	124	116	100	98

Source: P. Forsyth, R. Hill and C. Trengove, "Measuring Airline Efficiency", *Fiscal Studies*, Vol. 7, No. 1 (February 1986), pp. 61-81.

Table 4

INPUT PRICES, UNIT COSTS AND TOTAL FACTOR PRODUCTIVITY, 1983

Airline	*Input price index Qantas, 1975 = 100*	*Cost/output (adjusted) index Qantas, 1975 = 100*	*Total factor productivity index Qantas, 1975 = 100*
MAS	101.0	114.0	100.4
SIA	145.9	140.5	104.6
Thai	97.4	133.5	82.3
Garuda	85.1	136.5	71.2
Qantas	197.0	167.0	127.5
Canadian International	177.1	125.5	154.6
JAL	199.3	156.7	140.1
Pan Am	218.7	134.4	162.3
Air India	83.0	145.0	63.8
Pakistan International	73.7	137.3	58.4
SAS	200.2	176.7	113.4
BA	159.9	157.9	108.2

Source: D Brunker, C. Findlay and P Forsyth, "Comparative Advantage in Airline Services", Paper presented to the Economists' Conference, Adelaide, July 1989.

Table 5

COST MOVEMENTS, 1978-1988

	Real GDP/ capita 1988/1978 (1)	*Exchange rate value of of currency in dollars 1988/1978 (2)*	*Relative inflation* [a] *(3)*	*Real exchange rate movement* [b] *(4)*	*Cost increase in dollars 1988/1978* [c] *(5)*	*Input cost increase* [c] *1978-1988* [d] *(6)*	*Cost/ATK 1988/1978 (7)*	*Cost/ATK 1988/1978 (8)*
Malaysia	1.32	0.85	1.46	1.24	1.64	1.41	na	na
Singapore	1.77	1.12	0.83	0.92	1.63	1.40	1.03	0.61
Thailand	1.51	0.80	1.21	0.97	1.46	1.26	1.11	0.66
Australia	1.20	0.69	1.25	0.86	1.03	0.89	1.47	0.88
Canada	1.23	0.93	1.07	0.99	1.22	1.05	1.85	1.10
Japan	1.47	1.55	0.75	1.17	1.72	1.48	1.40	0.83
United States	1.16	1.00	1.00	1.00	1.16	1.00	1.68	1.00
India	1.22	0.56	1.36	0.76	0.93	0.80	1.10	0.65
Pakistan	1.40	0.57	1.21	0.69	0.97	0.83	1.30	0.77
Sweden	1.20	0.75	1.31	0.99	1.19	1.02	3.05	1.82
United Kingdom	1.19	0.91	1.43	1.30	1.55	1.33	1.43	0.85

Source: International Civil Aviation Organization, *Fleet and Personnel*, and *Financial Statistics*; International Monetary Fund, *International Financial Statistics.*

a Percentage price rise divided by percentage rise in United States.

b The real exchange rate change is the product of column (2) and column (3). A value less than 1.00 indicates a real exchange rate depreciation, which is a positive factor for competitiveness.

c Product of column (1) and column (4).

d Columns (5), (6) and (8) scaled to United States = 1.00

INTERNATIONAL TRADE IN TOURISM IN ASEAN REGION

*Chow Kit Boey**

INTRODUCTION

The objective of this paper is to identify areas for increasing the participation of domestic firms from the ASEAN countries in the international trade in tourism. Firstly, this paper analyses the market size and structure of international tourism in the ASEAN region. Due to the paucity of data and information on Brunei Darussalam, the paper covers only five ASEAN member countries - namely, Malaysia, Indonesia, the Philippines, Singapore and Thailand.[1] Secondly, the paper discusses the growth prospects and problems of international tourism in the region. Thirdly, the operations of four tourism sectors - hotels, tour operators, travel agents and air transportation - are examined with respect to the competitive positions of domestic firms vis-à-vis foreign firms. Fourthly, areas for increasing the "value-added" in tourism trade are suggested together with avenues for higher foreign-exchange earnings from tourism in ASEAN countries. The paper concludes by analysing the implications of the study's findings for the Uruguay Round negotiations on trade in services.

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1 Except on the number of visitors, hotels and tour operators and agents.

I. MARKET SIZE AND STRUCTURE

A. Size

The ASEAN region receives almost 4 per cent of the world's visitors. During 1987-1989, the inflow of visitors to ASEAN countries expanded at a compound rate of 12.8 per cent per year. Singapore and Thailand each recorded 4.8 million visitor arrivals in 1989, followed closely by Malaysia which reported an inflow of nearly 3.7 million. Indonesia and the Philippines had about 1.6 million and 1.1 million visitors respectively in 1989, while Brunei received about 0.1 million visitors.

Close to its share of the world's visitors, the ASEAN region captured 4.1 per cent of total world travel receipts in 1988 (table 1). In that year the travel receipts of Thailand surpassed those of Singapore. Compared to each country's gross output, travel receipts were highest for Singapore - 10 per cent of GDP. For the other ASEAN countries, travel receipts amounted to less than 5 per cent of GDP, except for Thailand, whose tourism revenue increased to 5.4 per cent of its GDP in 1988.

B. Composition

The top markets for ASEAN's tourism trade are mostly in the Asia-Pacific basin (table 2). Specifically, these markets comprise the ASEAN countries themselves, the other rapidly industrializing countries in East Asia, as well as Japan, Australia, the United States and the United Kingdom.

Singapore groups all ASEAN countries together in its statistics. Its rank orders of top markets are thus not strictly comparable to those of the other ASEAN countries. Malaysia and Indonesia have traditionally been Singapore's major markets, while Thailand has become a major source of tourists to Singapore in recent years. Taking this into account, the Philippines has the highest concentration (60 per cent) of tourists in terms of the originating markets: half of the visitors to the

Philippines are from the United States, Japan and Hong Kong.[2] By contrast, Malaysia has a more diversified source of visitors; less than a quarter of the visitors are from the five top markets. For Indonesia, Thailand and Singapore, over half of the visitors are from the five top markets.

Intra-ASEAN tourism is most significant for Singapore and Thailand and least significant for the Philippines. The only tourist-generating country which is among the top five for all ASEAN countries is Japan. Japan is also one of the fastest growing markets for three ASEAN countries - Malaysia, Singapore and Thailand. For Indonesia, Singapore and Thailand, European countries are becoming increasingly important. Three EC member States - Germany, France and Italy - have recently shown strong growth in travel to ASEAN.

C. Visitor profile

The majority of the visitors to the ASEAN countries come on holiday. At least, according to the declarations made by travellers, business visits account for less than 20 per cent of the total number of visits. Almost half of the visitors are below 40 years old. The largest occupational group of visitors comprises professionals, managers and technicians, except for Singapore where housewives and students form the largest group. On average, visitors to the Philippines stayed the longest (12 days) whereas those to Singapore stayed the shortest (4 days).

With the exception of Singapore and Thailand, visitors in the ASEAN region spend the most on accommodation, which takes up 27-47 per cent of the total expenditure. Reflecting the country's availability of goods, in particular brand-name items from Western Europe, visitors' expenditures on shopping in Singapore amount to 63 per cent of total expenditures. In Thailand, shopping absorbs 39 per cent of total expenditures of visitors.

Available data indicate that expenditure per visitor is the highest in the Philippines, partly due to the greater length of stay. In terms of

2 A large proportion of the visitors from the United States are overseas Filipinos.

daily expenditure, visitors to Singapore spend at most about $190 per visitor per day.

D. Formal restrictions

Restrictions on travel can be broadly classified into those measures which affect the travellers themselves and those directed to the provision of services to travellers. Under the first category are measures that:

- limit the amount of credit or cash that a resident or citizen can take out per trip. Thailand has recently raised its credit ceiling which effectively has little restrictive impact on expenditures abroad.

- limit the amount of purchases that can be brought back from abroad. Virtually all countries set limits on duty-free allowance. In addition, permits may be required for certain goods such as electrical items in Malaysia, while in some cases, the entry of certain goods is prohibited, as for example, refrigerators in India and Pakistan.

- limit overseas trips by making such trips more expensive, for instance, through a departure or exit tax. In Thailand, a 2.2 per cent tax on each airline ticket is imposed apart from an exit tax. The Philippines taxes departing residents travelling on first class more than those on economy class. Indonesia has recently liberalized its exit tax. From July 1990, exemptions from exit tax are granted to eight categories of travellers. Another measure making travel more expensive is Australia's Fringe Benefit Tax which requires the payment of a tax on the holiday/entertainment content of incentive travel by the sponsor of the travel awards.

- limit on the number of trips through foreign-exchange restrictions. Pakistanis can only travel once in two years on foreign airlines against Pakistani rupees. No restrictions are imposed on travel on the national carrier.

- discourages travel with strict and lengthy customs or immigration checks/procedures. Some ASEAN countries (Thailand, Indonesia

and Malaysia) have introduced green lanes for visitors who have nothing to declare. This has facilitated greatly the clearing of frontal procedures and eliminated the long queues which had led to congestion in the airport buildings.

Under the second category of restrictions on the supply of tourism services are:

- Restrictions on the establishment of wholly foreign-owned companies, leading to joint ventures such as in the case of travel agents in Indonesia.

- Restrictions on tourism promotion. Custom duties are imposed on promotional material. For instance, promotional material brought into Australia are taxed at 50-70 per cent of their cost. Tax exemptions are allowed on tourism-publicity material which contains less than 25 per cent commercial advertising and is distributed free. Foreign artists or performers for promotional events are required to pay fees to the Australian Musicians Union and Australian Actors Equity. Another form of restriction are taxes levied on production costs of promotional material or on printing costs. Yet another restriction is the ban on certain languages. Consequently a new set of promotional material needs to be produced in order to comply with the requirement, thereby increasing the cost of promotion.

- Restrictions on advertising. TV commercials produced overseas are prohibited as is the case in India, Pakistan and Malaysia. Restrictions on the composition of advertising crew for films exist in Australia. For advertising films, an Australian crew of at least four, including one from the Australian Actors' Equity, are required.

- Restrictions on tour guide services. Many countries - Italy, for instance - bans foreign tour guides. Others, for example Singapore, requires licensing of tour guides to control the quality of the service.

- Restrictions on the provision of transport-related activities. Ground handling services by non-national airlines are disallowed in many European OECD countries.

- Restrictions on promoting outbound travel. Indonesian travel agents promoting outbound travel are required to handle a larger proportion of inbound travel.

The above is not an exhaustive list of the formal restrictions on tourism services.[3] However, it may serve to highlight some major obstacles in international tourism trade.

II. GROWTH PROSPECTS AND PROBLEMS

One study has projected tourism receipts to grow at an average rate of 4 per cent a year for the decade 1986-1996.[4] World tourism receipts as a ratio of world gross product will rise from 11.2 per cent in 1986 to 12.2 per cent in 1996.

Forecasts for the Far East and Pacific region indicate an annual growth rate of 7 per cent for the 1990s decade.[5] Growth rates for the ASEAN countries range from a predicted low rate of 5 per cent for Singapore to a relatively high rate of 11 per cent for Indonesia.[6] The forecasts have taken into account the capacity constraints of two airports in the region - Japan's Narita airport and Hong Kong's Kai Tak airport - and inadequate hotel accommodation in Thailand and Hong Kong. The strong growth in some tourist destinations, for instance Thailand, Indonesia and Malaysia in the ASEAN region, is due partly to a strong consumer-preference for beach holidays. Some diversion of European tourists to the Far East and Pacific from traditional beach resorts in the Mediterranean is foreseen, as a result of the overcrowding

3 For details of other types of restrictions, see GATT document, "Trade in Tourism Services", MTN.GNS/W/61, 4 July 1989; and OECD, *Tourism Policy and International Tourism in OECD Member Countries* (Paris, OECD, 1987).

4 Somerset R. Waters, *Travel Industry World Yearbook: The Big Picture, 1988* (New York, Child and Waters, 1989), p. 11.

5 EIU, *Far East and Pacific Travel in the 1990s: Forecasts and Analysis of Potential and Constraints* (London, EIU, 1990).

6 Predictions for the rest are 8.5 per cent (Malaysia), 6 per cent (Philippines) and 9 per cent (Thailand).

and pollution problems the region. Other contributory factors to the attractiveness of the Far East and Pacific region are the predicted diminishing differentials between short-haul and long-haul air fares, and the continuing adverse factors in other competing holiday resorts.

Opinions on the major barriers or limitations to tourism growth in the ASEAN region reveal a common problem, that of an inadequate number of trained workers, especially in the hotel industry. Some measures have been initiated to counteract this situation. At the ASEAN level, a training programme sponsored by the European Community is viewed as a significant assistance welcomed by all the ASEAN countries. At the wider Asia-Pacific level, ESCAP's activities on human-resource development in tourism are one of the earlier efforts made in addressing the issue. National organizations are endeavouring to expand training programmes but the shortage of trained personnel at middle-management level and below could adversely affect the tourism industry in the mean time.

Another barrier to growth in tourism cited by most of the interviewees was the insufficient capacity of airports, airlines and other infrastructure. As noted earlier, congestion at Narita airport is one of the factors for a lower predicted growth rate. In the case of the ASEAN countries, the insufficient capacity of two national airlines has resulted in some negotiated air rights not being utilized. Paradoxically, another national airline in ASEAN has been less successful in obtaining more air routes. Apart from the expansion of congested airports, alternative airports are offered in bilateral negotiations for additional flights. Indonesia, for instance, is promoting less utilized destinations in the country. The eastern part of the country is targeted for tourism development, but the plans are being handicapped by the lack of capital for infrastructural construction.

Another major concern mentioned is conservation. It is noted that if no measures are taken to conserve the environment, pollution and damages to natural reserves will eventually reduce tourist inflows. On the other hand, conservation measures will hinder tourism growth. Indonesia has chosen the balanced growth route and is aware of the trade-off between short-term high growth and pollution in the tourism

trade. The carrying capacity of each tourist destination is being more seriously examined for tourism development.

One of the major barriers cited in Thailand is the lack of co-ordination in the administrative and regulatory systems related to tourism activities. It has been argued that the conflict of interests among authorities, agencies and departments has hampered various tourism services. Moreover, the absence of a supervisory body with commensurate power has led to problems not being solved swiftly and democratically.

In Indonesia, the small amount of promotion funds, and the even smaller amount of advertising funds, is viewed as a constraint to promoting and hence expanding tourism. One way to obtain promotion funds, as practised in Singapore, is to impose a cess on hotel accommodation, food and beverages. Such funds will fluctuate in line with the tourist cycle.

The lack of entertainment is noted as a cause of the short length of stay of tourists in some destinations. It is recognized that government regulations on tourism services have been liberalized in some sectors and places. Such measures have resulted in longer visits and it is foreseen that a relaxation of regulations in the entertainment sector is likely to follow.

Finally, tourism growth in ASEAN can be furthered through an intensification of regional co-operation. Although tourism is one of the first service sectors in which progress was made in regional co-operation, there remains much more that can be accomplished with greater collaboration. Tourism is an area where balancing the benefits among ASEAN countries is more easily achieved through inter-sectoral exchange of benefits since tourism covers many sectors - transport (land, water and air), hotels, restaurants, recreational, cultural and other entertainment services, tour operators and travel agents, financial and insurance services, real estate, retail services and handicraft industries.

1992 will be the "Visit ASEAN Year". The promotion of ASEAN as a tourist destination is not easy because the individual tourist spots and each member country are better known than ASEAN as a whole. ASEAN will be promoted as "The World's Six-in-One

Tropical Paradise", involving the difficult task of selling a package of six destinations, given the diverse tastes and preferences of visitors. Tour packages covering two or three ASEAN destinations will have to be accepted as an ASEAN package.

Fly-cruise packages are seen as a way to increase tourist inflows, while even though this may mean overstraining the existing capacities of airports, airlines and hotels. The expansion of cruise vacations in ASEAN could be a means of developing tourism in ASEAN region without incurring concomitant heavy expenditures on airport and hotel construction. Cruise packages are also expected to attract more repeat visitors to the region, particularly those who prefer variety in destinations.

III. COMPETITIVE STRUCTURES IN TOURISM SERVICES SECTORS

A. Hotels

Of the world's total number of rooms in the hotel sector - estimated at 10.5 million in 1988 - about three quarters are located in Europe and North America (the United States and Canada).[7] Hotel capacity in East Asia and the Pacific amounts to about 9 per cent of the world's total capacity.

Hotels in Asia and Australasia perform better than the world average in terms of occupancy rate. The median room rate in Asia and Australasia was close to that of Europe but below that of the world in 1986. More sales are made in food for hotels in Asian and Australasian and Europe compared to the world average. In terms of net income per room, Asian and Australasian hotels perform below the world average and much below that of Europe which has remained the highest.

The hotel sector in developing countries is dominated by international hotel chains originating in developed countries. The United States is the home country of the world's first hotel corporation, and its

7 Walters, *The Big Picture, op. cit.*

hotel corporations were the first to venture abroad after the Second World War. Vertical integration in tourism services has resulted in international hotel chains being linked to international airlines, tour operators or travel agents. As the major tourist-generating countries have traditionally been the developed countries, it is not surprising that international hotel chains originated in these countries.

The growth of the international hotel chains was based mainly on their management services and not on equity participation. Management services are provided through franchising, management contracts or licensing. In the past 20 years, management companies have grown and currently number over 600. One United Nations study indicated that in Asia 60 per cent of hotels affiliated with transnational hotel chains were linked by management contracts and 23 per cent by franchise, whereas only 15 per cent were linked by equity shares.[8]

The strong competition arising from the growth in management companies has brought about more favourable contracts for hotel owners. Apart from lower management fees, the new contracts offer higher equity participation by the management company, shorter contract terms and more qualifying clauses. In Thailand, for instance, Siam Intercontinental and Hilton International hold 30 per cent and 15 per cent equity respectively. In some cases foreign equity is at 49 per cent, the maximum allowed under Thai law. This is in striking contrast to traditional management contracts which are virtually no-risk, guaranteed minimum-income arrangements for the international hotel corporations. Traditional management contracts are of 20-25 years term whereas the new contracts are of 5-10 year periods, as is the case of Sheraton International.

Some indications of the extent of transnational hotel involvement in three ASEAN countries are available. The data show that the proportion of hotel rooms affiliated with transnational hotel chains is 44 per cent for the Philippines, 33 per cent for Singapore and 10.4 per cent for Thailand in 1979.[9] In Bangkok, 17.2 per cent of hotel rooms in 1988 were affiliated to transnational hotels. This share rises to 32.5 per cent

8 UNCTC, *Transnational Corporations in International Tourism* (United Nations Publication, ST/CTC/18).

9 *Ibid.*

for the deluxe and first class categories, reflecting the pattern of transnational hotel operation. Thailand is the host of 12 international hotel chains, of which 5 are listed in the world's top eleven. The regional headquarters of these chains are located in Hong Kong or Singapore where better telecommunication networks and other infrastructural services exist.

Besides international chains, there are regional hotel chains. The Asian chains include Mandarin Oriental, Mandarin (Singapore) International, Merlin Management International, Shangri-La International, etc. It has been observed that Asian chains "are similar in structure, operations and management" to international chains.[10] One reason is the mobility of international chain personnel within Asian chains, except in Japan and India where management is restricted to nationals.

Other participants in the hotel sector are independent hotels and local chains. Thailand has probably the largest number of local hotel chains in ASEAN. Among the "home-grown" hotel groups are Dusit Thani, Siam Lodge, Central, Royal Gardens and Imperial.[11]

As of 1989, the number of hotels in the ASEAN region with more than 50 rooms totalled 622. More than a third of them were located in Thailand (233), one quarter in Indonesia (164) and the remainder distributed among the Philippines (79), Singapore (71), Malaysia (68) and Brunei (7).[12]

There are 14 international chains and 19 regional chains in the ASEAN region.[13] International chains are defined as those hotel groups with world-wide operations while regional chains have hotels in some countries outside their home country. Twelve of the international

10 Murray Bailey, "International Hotel Chain Expansion in Asia", *Travel and Tourist Analyst*, March 1986.

11 For details, see Imtiaz Muqbil, "The Thai Tourism Industry: Coping with the Challenge of Growth", Asian Business Press Group, 1990.

12 Computed from Calton Pte Ltd, *Hotel and Restaurant Suppliers' Directory 1989/90*, fifth edition. According to the *Yearbook of Statistics, Singapore 1989*, there were 67 tourist hotels with 50 or more rooms at the end of 1988, and 63 hotels at the end of 1989. The above numbers serve to indicate the relative size of the hotel sector in ASEAN countries.

13 This does not include hotel groups based in Asia and the Pacific, with less than 3 hotels and all groups based outside Asia with less than 10 hotels.

chains are based in the West (eight in the United States, three in France and one in Switzerland) and two are based in Asia (Japan and Hong Kong). Sheraton will soon be the only world-wide chain represented in all six ASEAN countries, while Hilton and Hyatt manage hotels in all the ASEAN countries except Brunei.

Of the 19 regional chains, Mandarin Oriental (based in Hong Kong) is the only chain operating in all the ASEAN countries except Brunei. The composition of the chains by country of incorporation is the following: 6 Japan, 4 Hong Kong, 3 Singapore, 2 Malaysia, and one each from Canada, Spain, India and Australia. The three Singapore-based chains are Beaufort International (which is a spin-off from Regent International Hotels), Mandarin Singapore International and Pacific Hotels International. Mandarin Singapore began with a locally-owned and managed hotel and expanded its operations to Malaysia and China. The two Malaysia-based chains are Merlin Hotels and Ming Court Hotels International. While Thailand has the largest representation of international chains, Singapore has the largest representation of regional chains. In addition, the well-known Shangri-La chain, based in Hong Kong but owned by the Kuok Group of Malaysia, manages 13 hotels in the region and partly owns the Westin-managed Shangri-La in Hong Kong.

Local chains, i.e. hotel groups located in one ASEAN country and operating at least three hotels, include groupings of independent hotels of which there are three in the ASEAN region. Alliance formation is one way whereby independent hotels can compete more effectively with chain hotels. Such co-operative actions also exist among independent hotels in developed countries. Available information indicates that apart from groupings of independent hotels, there are 12 local chains in ASEAN: six in Thailand, three in Indonesia, and one each in Malaysia, the Philippines and Singapore.[14] Proportionately more local chains are family enterprises as compared to international and regional chains. Among them are Singapore's Goodwood group (Khoo family), Philippines' Sulo group (Enriquez family), and

14 Excluded are hotel groups which are not marketed as a group. For instance, the Hong Leong Group of hotels in Singapore comprising the Orchard Hotel, King's Hotel, Novotel Orchid Inn and Harbour View Dai-Ichi Hotel; and the group of hotels in Malaysia and China affiliated to Singapore's Hotel Equatorial.

Thailand's Central (Chirathivat), Imperial (Hoontrakul), Dusit Thani (Piyaoui), and Siam Bay and City (Sukosol).

ASEAN countries have had to rely on transnational corporations from developed countries as the principal sources of tourist flows and technology transfer. However, the growth of tourism has enabled ASEAN firms to gain bargaining strength. Management contracts are now negotiated on terms more favourable for ASEAN hotel investors. Over the past thirty years, more regional and local chains are taking a larger share of the tourism market.[15] Bangkok's Oriental Hotel and Singapore's Shangri-La Hotel are now well-known, reflecting the ability in the ASEAN region to gain a stronger foothold in the international tourism trade. Moreover, some international chain-affiliated hotels are now being locally managed, such as Thailand's Regent Cha-Am Hotel which was first managed by Hyatt. Of Bangkok's top five hotels, four are currently locally owned and managed. A way to obtain access to world-wide reservations systems by a local hotel has been demonstrated by Dusit Thani which is linked to JAL computerized reservation system. Another example is Singapore's Garden Hotel which has joined Best Western, one of the world's largest chain of independently owned and operated hotels. The chain has 3,200 members in 35 countries. Garden Hotel is expecting an increase in its occupancy rate through referred FIT (free, independent travellers) business from Best Western.

While management contracts are very specific on management fees, incentive payment, technical services, etc., they are less detailed on staff training. Generally staff are trained on the job. Given the acute shortage of trained personnel in the ASEAN region, it may be useful for governments to tie tax incentives for promoted firms with approved company-training programmes or to encourage in-company training programmes through subsidies or other conditions.

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15 It is not only in ASEAN that international chains are facing strong competition from regional and local chains. In the United States, they are moving into the budget segment and experimenting with "yield management" pricing. Originally adopted by the airlines, this system allows price to change in accordance with demand and relies heavily on a computerized reservation systems. See Waters, *The Big Picture, op. cit.*, p. 128.

B. Tour operators and travel agents

Similar to hotels, tour operations are capital-intensive and in some areas are heavily dependent on tourist-generating country firms. The market is segmented into tour operators specializing in inbound traffic, outbound traffic or both inbound and outbound tours. For outbound traffic, the tours offered are international, regional or single country. In the ASEAN region, some companies concentrate solely on pilgrimage tours to Saudi Arabia.

Little information is available on the size of the group travel market. An estimate for the United States indicates that about 2.6 million persons travelled to foreign countries in 1986 on pre-paid package trips.[16] In ASEAN, official statistics show that a high proportion of visitors on packaged tours are visitors from Japan, Hong Kong and Taiwan. Around one-third of the visitors from the five largest markets to ASEAN arrive through packaged tours in the case of Indonesia, the Philippines and Thailand. In the case of Malaysia and Singapore, visitors are mainly from neighbouring countrie, who generally prefer to travel on their own.

The ASEAN inbound tour market is dominated by big firms linked to transnational corporations from developed countries. Foreign firms tend to establish subsidiaries in countries where this is permitted. Otherwise, joint ventures are set up, or some other forms of affiliation are arranged.

In the industrial countries, many tour operators and travel agents are owners of transnational hotel corporations. Instances of similar forward integration in the provision of tourism services have been observed in the ASEAN region. One Thai travel firm, TRAC Travel, is building its own hotel after the frustrations encountered in obtaining hotel rooms during the recent hotel "profiteering" rate row.[17] The hotel will block 30 per cent of its rooms for the travel firm. An Indonesia travel firm went even further in building a hotel exclusively for its own customers; the rooms are not available to other travel companies. Yet

16 *Ibid.*, p. 124.

17 Muqbil, *op. cit.*, p. 90.

another form of integration within the tourism services sectors is exemplified by Singapore's Tradewinds. The company is leasing aircraft from the national airline for its own tours.

With the advent of computerized reservation systems, small firms with insufficient capital resources are increasingly being disadvantaged. Travel firms are using computer programmes for hotel allotments as well as for more efficient accounting and for prompt invoicing and payments.

Another development in the tour services sector which leads to the further growth of large firms is that these firms are now operating their own tours which were previously contracted out to smaller firms.[18] The increased volume of tours due to the phenomenal growth in tourism in the region allows for more economical operation of tours by the tour operators themselves. An additional benefit arising from this is the "free" advertising obtained from the tour buses carrying the company's name. Besides, the quality of tour service is more controllable under the company, and the leakage of revenue due to subcontracting is eliminated.

Tour operators are competing for the convention and incentive travel market, which is of higher value than the traditional pre-paid package tours. A problem encountered in convention operations is the customs clearing of convention material in some countries. Customs procedures may be lengthy and thus time-consuming. In some cases, the scope of tax-exemptions of convention materials is not clear.

With a buoyant tourism market, job hopping has steadily increased in the hotel, airline, and tour operator/agent sectors. These sectors have to compete for experienced staff by offering higher wages or better fringe benefits. Labour costs are increasing, thereby cutting into operating profits. Ironically, at the same time, some tour operators are undercutting tour prices unnecessarily.

In recent years, tour operators have been increasingly creative and imaginative in developing new tours to suit the differing tastes of tourists. The products are becoming highly differentiated, attracting

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18 *Ibid*, p. 101.

more repeat visitors to the country. Direct flights to the newly popular tourist spots have facilitated the conduct of the new tours.

Unlike the tour operator market, the travel agent sector comprises a small number of large agents and a large number of small agents. Statistics available for the United States show that independent travel agents make up 64 per cent of the total number of agency locations.[19] The world's largest travel agency is probably Europe's Wagon-lits. It acquired the United States' T.V. Travel in 1988. In co-operation with Thomas Cook by an agreement, Wagon-lits services are provided through 1,500 agencies in 136 countries.

Generally, regulations on the operations of travel agents in ASEAN are fairly relaxed. The ease of setting up a travel agency as well as the small amount of capital required have resulted in an increase in the number of small agencies. In this sector as well as in the tour operator sector, a strong case can be made for stricter government control to ensure better consumer protection. This is especially so, in the light of a recent study which revealed the operation of socially damaging tours by foreigners.

To the extent that larger firms in the tour operator and travel agent sectors are foreign affiliated, small domestic firms are competing at less advantageous positions because of the absence of linkages with tourist generating country firms. There are large domestic firms handling outbound traffic, some of which are entering the inbound traffic sector. A few are able to establish offices abroad, often managed by nationals who have migrated. A new subsector is being created, particularly in the travel agent sector, when domestic firms abroad attract returning nationals or former nationals to their services away from home-country firms.

According to a 1988/89 travel directory, there are some 1,300 tour operators and agents in the ASEAN region.[20] The breakdown is as follows:

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19 Waters, *op. cit.*, p. 123.

20 Interasia, *ATT Travel Directory 1988/89* (Hong Kong, Interasia, 1989). The coverage is incomplete as two other sources on tour operators and travel agents in Singapore indicate a total of 292 for 1987 (Department of Statistics, Singapore, *Report on the Survey of Services 1987*) and about 430 for 1989/90 (Singapore

Country	*Number of Firms*
Brunei	35
Indonesia	187
Malaysia	333
Philippines	231
Singapore	258
Thailand	294
Total	1,338

Owing to resource constraints and data availability, only the Singapore market is analysed further. As Singapore has no restrictions on foreign ownership and repatriation of profits, the Singapore market could be seen as a case of maximum foreign participation, given the economics of the travel trade.

The combined market of tour operators and travel agents is dominated by small firms. Nearly half of the firms have employment size of less than 10 employees, while only about one per cent are large firms with a staff size of at least 100. Almost all are private limited companies (99 per cent) and established within the last 25 years (97 per cent), i.e. after Singapore became an independent nation. Less than half (44 per cent) reported annual sales of S$1 million or more in 1987.[21]

Almost one quarter of the firms service both inbound and outbound traffic. Thirty per cent of the firms service inbound traffic only, while another 30 per cent operate outbound traffic only. A very small proportion (less than 10 per cent) are solely engaged in ticketing services. Some 60 per cent of the firms are affiliated to trade associations - national, regional or international.

Telecom, *Singapore Buying Guide*, July 1990). Figures from the Singapore Tourist Promotion Board are 388 agents in 1987 and 420 in 1988. The Directory is, however, useful for obtaining some market characteristics of travel suppliers.

21 The statistics are taken from the *Report on the Survey of Services 1987*. Data from the Singapore Tourist Promotion Board indicate a lower proportion of 30 per cent with sales of at least S$1 million. Other details in the following paragraphs are extracted mainly from the *Directory*.

From available public records, 33 foreign travel firms are identified. A large majority (70 per cent) of these firms are headquartered in Asian countries - namely, Malaysia, Thailand, Indonesia, Japan, Hong Kong and Taiwan, Province of China. Slightly over 40 per cent are small firms of less than 10 staff. The highest reported sales is almost S$30 million.

Among the domestic firms are 12 firms which have expanded overseas. Four firms have branches only in Malaysia. The rest have established branches in countries further away, and two of them have even entered the United States and United Kingdom markets. These firms are generally larger than the foreign firms. Only two firms have a staff size of less than 10, while the largest firm has an employment of over 300. The annual turnover of three firms has each been reported to be S$40 million or above. These big firms are tour operators and are thus larger than foreign travel agents in Singapore.

Another group of local firms has also been identified. These are domestic firms with branch offices in Singapore. These 37 firms have established branches in order to be nearer to the outbound markets. The data on some of these firms show that only a few firms are small, employing less than 10 persons. However, only one firm has a staff size of over 100, and none has an annual sales volume of S$20 million or more.

The total size of the industry has been estimated at S$2 billion in 1988.[22] This implies that the largest firm - a local company with foreign branches - grossing S$7 million of sales, captured 3.5 per cent of the market. More than half of the firms in the industry operate with less than S$1 million in annual sales. Given the keen competition for business resulting in high discount rates for the customers and low margins for the firms, the services provided by the firms are not generally considered to be satisfactory. Furthermore, in lean years, a large number of firms (42 per cent in 1986) operate at a loss. It seems unlikely for small firms to merge in Singapore to capture economies of scale, although there are linkages among some 100 firms through equity participation.

22 *Travel Trade Gazette Asia*, 16-22 February 1990.

To enhance their competitive edge, a few firms have formed alliances with foreign firms abroad. For instance, Franco-Asian Travel has concluded a partnership with Hickory, Siakson Coach Tours operates as the official Grayline of Singapore and Travelwell is the authorized agent for Intourist. A few travel agents are advertising jointly, thereby capturing greater public attention at lower costs.

Exemplifying an indigenous firm which has become a major participant in the travel industry is Chan Brothers Travel. Began in 1965 with only a staff of three engaged mainly in ticketing sales, the firm currently has an employment size of 150, offering a wide spectrum of services for outbound travel. The firm has representative offices in Thailand, Hong Kong, Taiwan, Japan, New Zealand, Australia, United Kingdom, United States and Canada. In 1989, it served more than 30,000 travellers to over 50 destinations. It was presented with the "Travel Agency of the Year - Outbound (Merit) Award" by the Singapore Tourist Promotion Board in 1987, and the Golden Kiwi Award in 1988 by the New Zealand Tourist and Publicity Office for being the New Zealand Agent of the Year in ASEAN. Another notable undertaking by the firm is its new training programme with the National Productivity Board to upgrade the skills of its employees.

Conceivably, high income growth will increase the demand for travel thereby offering much potential for ASEAN travel firms to expand, particularly in the outbound sector. Domestic travel firms in the ASEAN region have demonstrated an increasing capability to participate more fully in the international travel market. In the coming years, it is possible for ASEAN travel firms to become internationally reputed, if no new market restrictions are introduced.

C. Air transport

National airlines in the ASEAN region hold a large share of seat capacity for scheduled flights in their respective countries. This share varies from country to country, ranging from 72 per cent for Malaysian airlines to 22 per cent for Thai International. Malaysia shows the highest concentration in seat capacity - five airlines accounting for 90 per cent. Thailand has the lowest concentration, with its top five airlines holding 46 per cent of the total seating capacity. Cathay Pacific, Thai

International and Singapore Airlines hold substantial shares of seating capacity in the ASEAN countries.

World air traffic is currently dominated by airlines from two industrial countries - the United States, with a share of 17 percent and the United Kingdom, with 10 per cent.[23] The Pacific Basin is the fastest growing air transport market and is reported to have generated airline revenue of $10 billion in the mid-1980s.[24]

In the ASEAN region, one major constraint to tourism growth is the full capacity of airports and national carriers. Responding to the capacity constraint at airport hubs, governments have promoted higher utilization of secondary airports and encouraged more direct flights. Due to environmental concern, some airports are not opened 24 hours a day. This has further intensified the capacity constraint. The level of congestion is forecast to rise in most locations.[25]

At least two ASEAN countries - Thailand and Indonesia - are not able to realize all the rights of flights negotiated bilaterally, because of aircraft shortages. The fleet of airplanes cannot be expanded quickly as new planes are made to order. Even if the fleet can be expanded with second-hand planes, a shortage of flight crew will probably result. The acute aircraft shortage problem could be gauged, for instance, in Thai International utilizing only about half of its total rights. Moreover, Thai International accounted for 22 per cent of seat capacity at Bangkok's international airport in 1988, a smaller figure than that of 1987.

In its attempts to retain its market share in the short-term, Thai International has devised two innovative arrangements with foreign airlines.[26] One is the leasing of a 461-seat aircraft from Air France for a once-a-week, economy class flight between Paris and Bangkok. The aircraft, with Air France colours and crew, carries a designator of both airlines, TG/AF. Both airlines have reservations of 200 seats each for their respective tour operators who are offered fares about 25 per cent

23 Waters, *op. cit.*, p. 137.

24 *Ibid*, p. 138.

25 See Christopher Findlay and Peter Forsyth, "ASEAN Interests in Air Transport Services in the Uruguay Round", elsewhere in this volume.

26 These are cited in Muqbil, *op. cit.*, pp. 73 and 75.

below the market rates. This arrangement stimulates new tour packages of one week or longer duration. The other arrangement is the conversion into scheduled flights of the charter flights to Phuket of an Austrian private airline, Lauda Air. The agreement, however, is made with Qantas and the flights are coded TG/QF. Lauda Air has no flight rights and can sell a portion of the seats that remain after allotment to Thai International and Qantas.

Another recent development in the air transport sector is the share swapping between Singapore Airlines and Delta Airlines of the United States. Joint services between the two airlines include joint fares, flight schedules, and one check-in between Singapore and Dallas. A second similar alliance, between Singapore Airlines and Swissair, is being worked out. These arrangements facilitate travel, and also result in the formation of chains and networking.[27]

Computerized reservation systems developed by groups of airlines are playing an increasingly important role in the provision of air transport services. These systems allow for easier planning of flight itineraries. Participation is priced at a fixed fee plus a variable cost proportional to usage. It has been observed that the positioning of flight information determines, to a great extent, the selection of flights. Travel agents make 85 per cent of their reservations from the first screen; the first line of the first screen captures 66 per cent of reservations.[28] It is therefore important to ensure that there is a fair listing of flight information and, in particular, that no airlines is discriminated against because of its listing position.[29]

Four ASEAN airlines and two airlines in the region have founded the Abacus CRS.[30] Recently an equity swap agreement was

27 See Findlay and Forsyth, *op. cit.*, for a discussion of the air transport alliances in which ASEAN airlines are involved.

28 Albert Bressand, "Access to Networks Services Trade: Uruguay Round and Beyond", in UNCTAD, *Trade in Services: Sectoral Issues*, (United Nations Publication, UNCTAD/ITP/26), p. 240.

29 See, for a discussion of the problems posed by biases in the computerized reservation systems, Murray Gibbs, Michiko Hayashi and Udaya Kumar, "Strenghtening Service Sectors in Asia and the Pacific: Overview and Conclusions", elsewhere in this volume. See also Findlay and Forsyth, *op. cit.*

30 The owners of Abacus are Singapore Airlines, Cathay Pacific Airways, China Airlines, Malaysia Airlines, Philippine Airlines and Royal Brunei Airlines.

concluded between Abacus Distribution Systems and Worldspan Travel Agency Information Services. Worldspan was formed by the merger of PARS and Datas II which were acquired in early 1990 by affiliates of Delta Air Lines, Northwest Airlines and Trans World Airlines. Plans are underway to link Abacus with the Infini system, which is a new CRS joint venture of Abacus and All Nippon Airways.

One main uncertainty in the air transport sector is the impact of the formation of a single market in Europe in 1992 on non-European airlines.[31] If the European Community negotiates on traffic rights as one entity, access to the Community's destinations will become difficult for non-member airlines. ASEAN could perhaps also choose to negotiate as an entity, treating intra-ASEAN flight sectors as domestic traffic. It has been suggested that liberalization within the European market on tourism may not result in rapid or marked changes in the Asia-Pacific region.[32] Gradual changes from increased competition will diffuse to other regions. However, the Federal Republic of Germany, the United Kingdom, France and Italy will remain the major markets for the Asia-Pacific region.[33]

IV. ENHANCING VALUE-ADDED AND FOREIGN EXCHANGE EARNINGS

Quality service is the key to increasing value-added in tourism services. Quality service is synonymous with fast and competent service. Efficiency and speed - both in drawing up a travel itinerary satisfying the client's preferences and in confirming flight and hotel reservations - are crucial to remaining competitive in tourism services. Hence, access to information networks is critical to firms operating in the tourism trade. Given the different networks that have been developed, it has been suggested that co-operative efforts of both governments and private sectors be directed at creating "some interface between the different networks and the ability of the final customer to

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31 See Findlay and Forsyth, *op. cit.*

32 PATA, *Europe 1992: Impact of a Single Market on Travel to the Pacific-Asia Area* (California, PATA, 1990).

33 This applies to ASEAN also.

choose and access any of them through a shared terminal and a common gateway".[34]

Competent service is obtainable through proper training. The rapid growth in tourism in the ASEAN region has resulted in a strong demand for personnel. Unfortunately, the training institutes have not been able to meet this growth in demand. The resultant tight labour market has led to job-hopping and minimal training including on-the-job training. Consequently, disruptions to the efficient operation of firms in the tourism sectors are frequent. Staff promotion is often not based on competence but rather due to the need to fill a position. The low level of experience of the staff has necessitated employing more persons. This problem is particularly serious in countries encountering a general shortage of labour.

Under such circumstances, the training of trainers is a more rapid way to build up an adequate pool of trained manpower. Proper supervision at work is another way to ensure skill formation. Refresher courses are required in sectors experiencing rapid changes in the operation systems.

The market structures of tourism sectors in ASEAN have a strong foreign component. There are large transnational hotel chains, transnational travel agencies, and transnational corporations in financial, insurance and other tourism-related activities. Over time, large domestic firms have acquired the capability to compete effectively with foreign firms. Regional and local hotel chains, for instance, have evolved. Some domestic travel agencies are even able to compete with foreign firms in the latter's home country. Competition between domestic and foreign firms is intensifying and is likely to spread to the home countries of foreign firms, if no restrictive measures are imposed on the establishment of firms and/or on the provision of services.

With the growth of domestic firms, more foreign exchange earnings from tourism will be retained in the host countries. The leakages of foreign exchange earnings due to imported components in the provision of tourism services vary in each ASEAN country accord-

34 Albert Bressand, *op. cit.*, pp. 240-41.

ing to its economic structure and according to the spending pattern of visitors. Singapore has the highest import leakage, mainly because of the absence of an agricultural sector and the shopping preferences of its visitors for goods produced in the West. In the other ASEAN countries, import leakages are lower because of the availability of domestic resources and locally produced shopping goods, including handicraft items.[35]

Of the various tourism sectors, the hotel sector is an area where import leakages can be reduced in several ways. In the construction of hotels, measures can be taken to employ local architects, engineers, project managers and other technical staff. In some cases, foreign personnel have been engaged instead of locals because of the former's reputation. Therefore, adequate opportunities need to be made available to local experts. Therefore, it might be worthwhile for hotel investors to be bold in trying out unknown professionals. In return, they can get lower costs for their projects.

Construction materials for hotels can also be sourced locally. This will foster the development of subcontracting industries. Linkages in the economy are strengthened and the multiplier effect is enhanced. The same applies to other inputs in the operation of the completed hotels.

Instances of reduced import leakages in ASEAN countries have been observed. A case in point is the establishment of a hotel by a tour-operator firm, eliminating its dependence on foreign affiliated hotels for its clients' accommodation. Another example is the entry of local tour agencies into the inbound tourist market after they have successfully developed their outbound operations.

The above are some ways whereby domestic firms in ASEAN can capture a larger market share and improve the country's net foreign

35 A recent study on Thailand indicated a net foreign exchange of 88 per cent of gross earnings in 1985. Faculty of Economics, Chulalongkorn University, "Study on the Economic Impact of Tourism in Thailand", prepared for International Trade and Tourism Division, United Nations ESCAP, Bangkok, 1990, p. 70. Available data for Singapore showed a net foreign exchange earnings of 51 per cent (1987) and for the Philippines, 83 per cent (1978). United Nations/ESCAP, "Expert Group Meeting on the Measurement of the Economic Impact of Tourism by Input-Output Analysis", Bangkok, November 1988.

exchange earnings from tourism. However, foreign firms and foreign products should be present to some extent to stimulate competition and to offer a wider range of products to the consumers.

V. IMPLICATIONS FOR URUGUAY ROUND NEGOTIATIONS

Tourism services are produced by several sectors in the economy. A number of such sectors, including banking, insurance, construction, telecommunications and transport, are specifically being considered in the Uruguay Round negotiations on trade in services.

The analysis of the hotel, tour operator and travel agency services in ASEAN reveals market structures that contain some oligopolistic elements. However, these have not proven strong enough to suppress competition. Foreign firms operating in these sectors are subject to government rules and regulations which cover the whole economy and are not specific to tourism. This is the same for ASEAN firms establishing operations in foreign countries.

Government regulations that affect tourism are mostly restrictive measures on travel, on expenditure and on promotional activities. Restrictions on promotional material can be covered by negotiations on trade in goods, while restrictions on the employment of personnel for promotion projects can be negotiated as part of labour services. Restrictive measures on travel and on travel expenditure have recently been liberalized in some countries following improved economic conditions and balance-of-payments situation. Except for a few countries, developed-country governments are in general less restrictive than developing-country governments on international travel.

As for restrictive practices or unfair competition in the provision of tourism services, those on computerized reservation systems fall under the network sector while those on airline and related services are under the domain of the International Civil Aviation Organization. Other than these two areas, no major restrictive behaviour has been observed in the operations of hotels, tour operators and travel agencies. More effective action needs to be taken by governments to protect the physical and social environments.

In the ASEAN region, the major problems encountered in tourism are related to infrastructures and manpower, rather than to discriminatory or restrictive practices. The strong growth in the tourism trade and the optimistic forecasts for the Asia-Pacific region are increasingly attracting foreign firms to expand in the region. There may be attempts to negotiate for more favourable treatment of foreign firms. In such instances, host-country governments can actively try for cross-sectoral exchanges.

For ASEAN firms to increase their participation in the international travel market, a larger pool of trained and competent personnel is required. Though ASEAN domestic firms have demonstrated their capability to expand abroad, further business expansion is constrained by skilled manpower shortages. The governments could play a more active role in initiating, facilitating and subsidizing training programmes in the hospitality sectors.

Presently, developing-country firms are heavily dependent on developed-country firms in the tourism trade. This is primarily because developed-country firms are already well-established in the tourism market and because of the large portion of tourists orginating in developed countries. As international travel becomes increasingly more common in developing countries, there will be greater opportunities for the growth and expansion of developing-country firms. In this way, the interdependence between developed and developing country firms will be more balanced, and the market share of developing countries in world travel receipts will be larger.

To conclude, from the experience of ASEAN, negotiations in the Uruguay Round on tourism could focus on restrictions on travel, currency allowance, purchases abroad, promotion materials, advertising materials and personnel. There should also be adequate safeguards to protect the physical and social environments of host countries.

Box 1

TRADE IN TOURISM SERVICES

Statistics compiled by the World Tourism Organization (WTO) show that international trade in tourism has registered a steady year-to-year growth in the past thirty years. Tourism, comprising leisure as well as business travel, ranks third as an export after oil and petroleum products, and automobiles and car components. Leisure travel, relatively price-elastic and not destination-specific, accounts for two-thirds of world tourism, while obligatory travel (e.g. business, family, study, pilgrimage, sport, etc.), less price-elastic and more destination-specific, accounts for the remaining one-third. If one were to include domestic tourism as well in the statistics, travel and tourism industry would emerge as the largest industry in the world in terms of both employment and sales. Like in several other services, in tourism too transnational corporations play an important role. However, unlike many other services, small and medium size businesses are very important in the provision of tourism services.

The share of developing countries in world-wide tourist receipts is estimated at a little over 23 per cent in 1989. Developing countries have shown considerable interest in the development of tourism for a number of reasons. These include the reliance of tourism on unspoilt and renewable resources, the importance of the sector in generating foreign exchange, the relative ability of developing countries to export tourism services, and the role of the sector in countering flight from the countryside, thus promoting a more balanced regional development. Furthermore, tourism may be developed so as to use predominantly locally-produced inputs, thus minimizing import content, as for example in India. However, in some countries - e.g. the Caribbean islands - such import substitution is rather difficult. The level of investment required in tourism in order to generate employment is lower than in other sectors.

Tourism is not a unified service sector, but rather a combination of a number of different services such as transport, meals, accommodation and entertainment. The packaging of these components itself constitutes a further service, namely travel agents and tour operators. Some of these service sectors are already under discussion within the Group of Negotiations on Services (GNS). Among them, transport is indeed the most important sector in determining the development of tourism. Likewise, tourism development has significant implications for the future development of international transport, particularly air transport.

In relation to the possible liberalization of international trade in tourism services, there are two issues that are particularly important - i.e. the promotion of trade in tourism, and facilitation of the flow of tourists across international borders. The latter encompasses issues related to passport and visa formalities and foreign exchange restrictions. These questions have traditionally been addressed by WTO, Since the launching of the Uruguay Round, WTO has consulted its Members concerning the perspective in which they view the liberalization of trade in tourism services.

A first series of consultations with European countries considered the conditions for and the possible consequences of the inclusion of international tourism within the GATT negotiations. The European countries identified a number of obstacles to international trade in tourism. Non-transparency and difficulties in market access were seen as "moderately serious" obstacles, while failure to observe national treatment and the unequal treatment between foreign enterprises were perceived as "slightly serious" obstacles. European countries identified the following areas of difficulty as encountered by firms in establishing and developing trade in tourism: staffing, transfer of funds, acquisition of land, establishment of branches, selection of business partners and suppliers, taxation and fiscal matters, access to local financial markets, pricing policy, and distribution, publicity and reservation networks.

WTO's consultations with developing countries have taken place on a bilateral basis, and there has not yet been any formal survey of opinion comparable to the European case. However, the developing countries have stressed the need to correct the imbalances in benefits to developed

Box 1 (Continued)

TRADE IN TOURISM SERVICES

and developing countries arising from international trade in tourism. Such a correction should lead not only to an increased flow of tourists to developing countries, but an increase in the developing-country share of receipts generated by tourism. The developing countries raised a number of issues as crucial to such a correction of imbalances. They include: reciprocity with respect to hotel capacity, elimination of unreasonable technical barriers to trade in tourism services, access to reservation networks and the objective listing of such systems for enterprises from developing countries, infant-industry protection for developing countries beginning to develop their tourism sector, access to education and training, procedures for establishing tourist representations abroad and freedom to deploy regular personnel abroad while developing tourist capacity, access to industrialized-country media for marketing tourist products, and addressing the anti-competitive practices of private operators.

The European countries had also identified some measures as important for improving developing-country participation in international tourism services. Access to information and reservation networks, assistance in strengthening domestic tourism services, and access to distribution channels, education and training were among such measures. WTO has noted that some degree of consensus exists between developing and developed countries on the modalities for increasing developing-country share in international tourism.

Box 2

TOURISM IN THE URUGUAY ROUND

Although most travel takes place between developed countries, travel is the one service indicated in the balance-of-payments accounts where a large number of developing countries show a surplus, and for many, particularly small and island developing countries, the most important source of export earnings, far in excess of any other good or service. For such reasons, "tourism" was often considered as a sector of interest to developing countries. When the sector was submitted to scrutiny by the Group on Negotiations on Services (GNS) it became apparent that the sector was dominated by developed-country airlines, hotel chains, car-rental agencies, tour operators, travel agencies, etc. A background paper submitted by the delegation of Mexico in July 1989 observed that there were factors other than labour and geographical endowment which determined competitiveness in tourism. These include: (i) it is not holiday tourism but rather business tourism that is prevalent; (ii) international air traffic is dominated by airlines from developed countries; (iii) airlines have increasingly large interests in other tourism activities like hotels, travel agencies and car-hire firms, and thus channel tourists toward the place where their interests may best be catered for; (iv) developed-country airlines and hotel chains control world-wide information and reservation networks; (v) the sector has become an activity that is intensive in capital, organization, information and know-how. Therefore, one could not speak of comparative advantage for developing countries in trade in this sector. It became clear that two aspects of "tourism trade" would have to be addressed: (a) trade relating to the movement of the travellers themselves, and (b) trade relating to the provision of tourist services abroad by national firms. The major developed countries were clearly the "demandeurs", seeking to reduce barriers to the movement of consumers, and restriction on their purchasing power, but primarily to facilitate the penetration of their enterprises (e.g. the hotel chains etc.) in destination countries, of which developing countries are becoming considerably important.

A Working Group on Tourism Services was set up under the GNS in order to examine framework principles and the need for a sectoral annotation. One problem encountered by the Group was the confusion with respect to the scope and definition of tourism services, as the sector covers activities which also fall under other service sectors such as transport, financial and telecommunications services.

An attempt to classify tourism-related services was undertaken by the GATT Secretariat in collaboration with the World Tourism Organization. In addition to conventional tourism services like transport, accommodations and travel agents, the classification included financial intermediation for travellers' cheques sales and services, vacation and travel loans, travel insurance, and tourism-related business activities such as rental/lease of tourist property, property management, tourism business and management consultancy, and advertising. While developing countries genrally maintain liberal regimes, they are worried that concessions to progressively liberalize the "tourism sector" not provide a means for developed countries to obtain market-access for what are essentially financial and business services, without negotiating concessions in these sectors. They have also been stressing the asymmetry of capital and labour flows, seeking freer movement of labour within the network of tourist enterprises. It is likely that liberalization in the tourist sector will involve specific concessions with respect to various sub-components to be included in the schedule of concessions.

The application of the most-favoured-nation clause in other sectors is confronted by the fact that most countries have entered into bilateral and plurilateral agreements in tourism and tourism-related matters aimed at facilitating their mutual tourist trade. Solutions proposed have included grandfathering of such agreements, bringing them into conformity with general framework obligations, and phasing them out within a limited time framework.

Box 2 (Continued)

TOURISM IN THE URUGUAY ROUND

The objective of developing countries is not only to obtain a greater flow of tourists to their countries but to acquire a more important share of the value-added generated. The tourism sector is where the concept of access to information networks, recognized at the Uruguay Round Mid-Term Review as a component of achieving effective access to world markets for developing countries, is crucial. Access to computerized reservation systems and other information networks is essential for the very survival of firms in this sector, along with access to information and to technology and training facilities. [a] This situation also lends itself to the resort to anti-competitive practices by private firms. [b] Developing countries have stressed that the application of the multilateral framework to the tourism sector would have to take into account their needs in these respects.

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a See Francoise Carrer, *America Latina y El Caribe: El Comercio de Servicios en Tourismo y las Negociaciones de la Ronda Uruguay*, (UNCTAD/CEPAL/PNUD, forthcoming).

b Philippe Brusick, Murray Gibbs and Mina Mashayekhi, "Anti-Competitive Practices in the Service Sector" in UNCTAD, *Uruguay Round: Further Papers on Selected Issues* (United Nations Publication, UNCTAD/ITP/42), pp. 129-56.

Table 1

TOURISM RECEIPTS OF ASEAN
(Million dollars)

Country	*1986*	*1987*	*1988*
Indonesia	642.57	921.96	1,286.13
	(0.86)	(1.32)	(1.55)
Malaysia	647.61	713.79	767.37
	(2.35)	(2.23)	(2.22)
Philippines	649.94	459.04	404.52
	(2.11)	(1.33)	(1.03)
Singapore	1,766.82	2,088.30	2,398.89
	(10.08)	(10.50)	(10.01)
Thailand	1,419.53	1,943.45	3,117.88
	(3.40)	(4.09)	(5.38)
ASEAN	5,126.47	6,126.54	7,974.79
World	130,100.00	158,700.00	195,000.00
ASEAN share in world (per cent)	3.94	3.86	4.09

Source: International Monetary Fund, *Balance-of-Payments Statistics*, Vol 40, Part 1, 1989; International Monetary Fund, *International Financial Statistics*, 1989; World Tourist Organization, *Yearbook of Tourism Statistics*, 1988, Vol. 1.

Note: Tourism receipts exclude air fares.

Figures in brackets are travel receipts as a percentage of the country's GDP.

Table 2

TOP FIVE TOURISM MARKETS FOR ASEAN
(Rank order)

Major markets	*Malaysia*	*Indonesia*	*Philippines*	*Singapore*	*Thailand*
ASEAN				1 (27.7)	
Malaysia		4 (8.5)			1 (19.9)
Singapore	1 (6.8)	1 (18.2)			4 (6.5)
Thailand	2 (7.0)				
Japan	3 (4.6)	2 (12.3)	2 (17.4)	2 (16.3)	2 (10.7)
Australia	4 (2.8)	3 (12.2)	4 (5.4)	3 (8.6)	
United Kingdom	5 (2.6)			4 (6.1)	
United States		5 (7.6)	1 (20.3)	5 (5.4)	5 (5.6)
Hong Kong			3 (12.8)		3 (9.0)
Taiwan, Prov. of China				5 (4.3)	
Share of top 5 in total (per cent)	(23.8)	(58.8)	(60.2)	(64.1)	(51.7)
Intra-Asean share of top 5 (per cent)	(13.8)	(18.2)	(0.0)	(27.7)	(26.4)

Source: *Travel Industry World Yearbook: The Big Picture, 1988*, Waters, Vol. 32.
Note: Figures in brackets are the percentage shares in total number of visitors.

Table 3

SHARE OF TOUR MARKET IN ASEAN, 1988
(Percentage)

Top five markets	*Malaysia*	*Indonesia*	*Philippines*	*Singapore*	*Thailand*
ASEAN				9.7	
Malaysia		52.6			17.9
Singapore	9.5	17.1			25.1
Thailand	10.5				
Japan	41.4	53.0	41.6	69.4	56.4
Australia	28.1	29.2	13.7	15.8	
United Kingdom	9.6			12.8	
United States		18.1	8.8	19.8	25.1
Hong Kong			57.6		62.2
Taiwan, Prov. of China			43.9		
Tour market of top 5	11.8	32.3	31.7	26.9	35.2

Source: *Travel Industry World Yearbook: The Big Picture, 1988*, Waters, Vol. 32.

TRADE IN SERVICES IN THE PACIFIC ISLAND COUNTRIES

*Yee Che Fong**

INTRODUCTION

This paper examines trade in services in the Pacific Island countries and focuses on the following aspects:

- The importance of services in their economies and trade;
- The possibilities of increasing the export of services as well as opportunities for developing new services in the region;
- The competitive situation of local firms vis-à-vis those from outside the area; and
- The possible impact of the Uruguay Round negotiations on trade in services and post Uruguay Round sectoral negotiations.

The term "Pacific Island countries" in this paper refers to the following countries: Fiji, Kiribati, Nauru, Papua New Guinea, Solomon Islands, Tonga, Tuvalu, Vanuatu, and Western Samoa.

In the light of the ongoing negotiations in the Uruguay Round and in the absence of a commonly-accepted definition of services, this paper will attempt to take into account all the major elements which constitute the invisibles component in the foreign exchange earnings and the main activities in the Gross Domestic Product (GDP) of the Pacific Island countries. These are the following: utilities; construction;

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wholesale and retail trade; restaurants and hotels; transport, storage, and communications; finance, insurance, real estate, and business services; community, social, and personal services.

Data and information used in this paper are from the South Pacific Forum Secretariat, the Tourism Council of the South Pacific, the South Pacific Commission, as well as those from national sources including interviews. Relevant data and information published by ESCAP, IMF, IBRD, and the Commonwealth Secretariat have also been used.

I. AN ECONOMIC OUTLINE OF THE PACIFIC ISLAND COUNTRIES

The Pacific Island countries, with a total population of six million, cover no less than half a million square kilometres of land and thirty million square kilometres of sea area. They are widely scattered and include a variety of comparatively medium and small developing economies, some of which are resource-deficient while others are rich in timber and minerals. The people depend for much of their livelihood on subsistence agriculture and fishing. Most consumer and capital goods are imported. Generally, the countries lack financial resources and depend to a varying degrees on foreign aid and some on remittances from abroad to sustain their living standards. Their national incomes vary widely as indicated by table 1.

The main exports of the Pacific Island countries are agro-based in nature: copra, coconut products, vegetable oils, fish and marine products, cocoa, coffee, vanilla, sugar, bananas, taro, vegetables and tropical fruit. Timber, gold, copper and other minerals are exported from Papua New Guinea, Solomon Islands, Fiji, Western Samoa, and Vanuatu. Handicrafts are exported from most countries. Manufactures comprise a relatively small proportion of their national exports, canned fish, beverages, garments and foodstuffs being the main items. As indicated by table 1, many of these countries import more than they export. Earnings from tourism, philatelic stamps, numismatic coins, remittances from abroad and aid (international and bilateral) help to supplement national earnings.

While the Pacific Island countries share a number of common characteristics, there are also market differences. For instance, some of them like Papua New Guinea, Solomon Islands, and Fiji have substantial mineral resources and population base which accord greater economic potential than others in the region. For the coral nations of Kiribati and Tuvalu, there are no natural resources other than the sea and their long-term prospects hold little more than services and remittances from citizens working abroad. Midway in the spectrum are countries like Tonga, Western Samoa and Vanuatu which have embarked on industrial, agricultural and tourist development, but remain constrained by the lack of natural resources, capital funds, expertise and to a certain extent, by systems of traditional land ownership and use.

The main components of the Pacific Island countries' economies may be summarized as follows:

- *Fiji*: Sugar, tourism, fishing, gold, timber, copra and manufacturing.
- *Kiribati*: Copra, salt, fishing and labour remittances.
- *Nauru*: Phosphates and mining.
- *Papua New Guinea*: Mining, timber, coffee, cocoa, palm oil, copra and fishing.
- *Solomon Islands*: Fishing, timber, copra and palm oil.
- *Tonga*: Copra, bananas, vanilla, fishing, tourism, labour remittances and aid.
- *Tuvalu*: Fishing, copra, philatelic stamps, numismatic coins and aid.
- *Vanuatu* : Copra, tourism, cattle, marine products and aid.
- *Western Samoa* : Copra, cocoa, vegetables and fruits, tourism, and labour remittances.

Amongst the Pacific Island countries, Kiribati, Tuvalu, Western Samoa and Vanuatu are on the United Nations' list of least developed coun-

tries, thus enabling them to obtain more preferential treatment in trade as well as aid.

Historical ties and geographical proximity tend to influence the orientation and economic interests of the Pacific Island countries. Recent regional trade and investment initiatives such as the South Pacific Regional Trade and Economic Co-operation Agreement (SPARTECA), and the Pacific Islands Industrial Development Scheme (PIIDS) tend to enhance the strong economic links of these countries with Australia and New Zealand, although there is growing interest in developing economic and trade relations with countries outside the region.

The traditional, economic and political ties with the metropolitan powers have also meant that the transport and communications facilities of the various Pacific Island countries tend to be more developed with Australia, New Zealand and Europe than they are internally within each country. Thus for example, Fiji, Tonga, and Western Samoa have better communications links with New Zealand than they do with each other, while Papua New Guinea has better links with Australia than with neighbouring Asian and Pacific countries.

Political and economic considerations have also helped to promote strong links between Australia and New Zealand on the one hand and the Pacific Island countries on the other. As major investors, Australian and New Zealand companies maintain an important presence in the economies of these countries in manufacturing, banking, insurance, commerce, hotel, aviation, shipping, advertising, entertainment and other service industries.

II. SERVICES IN THE NATIONAL ECONOMY AND TRADE OF PACIFIC ISLAND COUNTRIES

In evaluating the significance of services in the national economy and trade of the Pacific Island countries, an examination is made in relation to Gross Domestic Product, employment and international transactions. With the exception of Nauru, all the other countries depend to a large degree on services for their national output. Business and community services, finance and banking, insurance, wholesale and

retail trade, restaurants and hotels lead the contributions to the services sector. Nauru, which is entirely dependent upon phosphate mining for its economic well-being, has a relatively minor service sector in hotels, restaurants, banking and government services. Although the agricultural sector is important in the economies of the Pacific Island countries, particularly for the large rural/village-based population, the services sector dominates the economies of most of these countries.

Table 2 shows the relative importance of the services sector in the Pacific Island countries. It is to be noted that with the exception of Nauru, Papua New Guinea and Solomon Islands, the services sector generates more than half of the GDP of the Pacific Island countries. Table 2 also shows the sharp rise of the services sector in most of those countries since 1970. Particularly significant are countries such as Fiji, Kiribati, Tonga, Western Samoa and Vanuatu where tourism, shipping and communications, business services, banking, shipping registry and international finance (tax haven) have been developed. Other developments such as the development of philatelic stamps bureaux have also led to the growth of the services sector. In Tuvalu, for instance, the sale of philatelic stamps is an important activity. The stamps bureau is also the largest employer in that country.

The importance of the services sector in the economies of the Pacific countries is also reflected in the employment structure of these countries as illustrated by table 3. The percentage of workers in services differs from country to country and ranges from 95 per cent in Tuvalu to 14 per cent in Papua New Guinea and Nauru. It is envisaged that in future the service sector will be expected to provide more employment for the population in most of the resource-scarce countries. In the case of Nauru, the services sector could become the mainstay of the country's economy once the phosphate deposits are exhausted in a few years time. For those countries endowed with timber, mineral and petroleum resources such as Papua New Guinea and Solomon Islands, the prospecting and exploitation of these resources would among other things generate demand for various services, thus creating more employment opportunities in this sector. Overall, the leading employment providers in the service sector are the following: community, social and personal services; commerce, including hotels and restaurants; transport and communications; and construction.

With regard to international trade, services occupy a prominent position in the total export of goods and services in almost all the Pacific Island countries. As indicated by table 4, earnings from services exceed that of merchandise exports of these countries with the exception of Papua New Guinea and the Solomon Islands. The export of services is particularly dominant in Kiribati, Tonga and Vanuatu which have practically no natural resources. Table 5 helps to further demonstrate the significance of services in percentage terms in the international trade of goods and services of the Pacific Island countries.

Services also figure prominently in these countries' imports but their magnitude is not as great as on the export side. It is to be noted that those countries like Papua New Guinea and the Solomon Islands which are comparatively small exporters of services have a larger proportion of services in their total import mix than other countries and they suffer deficits in the international trade in services as compared to surpluses made by the rest of the Pacific Island countries.

Services activities in addition to their importance in national output and international trade also provide a strong impetus for national growth in the Pacific Island countries, particularly at times when other sectors like agriculture and manufacturing do not seem to do well. During the years 1980-85, tourism, business services, transport and communications provided growth, while other sectors seemed to lag.

III. KEY SERVICE ACTIVITIES AND INTERNATIONAL TRADE

This section examines the provision of key service activities in the Pacific Island countries including their prospects for growth and ability to compete. The activities described include: tourism, transport and shipping, telecommunications, banking and financial services, and other business services including overseas labour.

The Pacific Island countries have an abundance of sun, sea, and sandy beaches which their governments and private sectors have utilized successfully to attract foreign tourists. In recent years, tourist arrivals in the Pacific area have been estimated at about one million per year with no less than 400,000 going to the Pacific Island countries. The

Asia and Pacific regions are the fastest-growing destinations of international tourism, and Pacific Island countries are expected to share in this growth in the future. While political bad weather conditions have caused a temporary slowdown in the growth of tourism in some of the Pacific Island countries, tourist arrivals have in general shown a significant increase over the past five years, especially for Western Samoa, Tonga and Papua New Guinea. Increase in tourist numbers have led to growth in the hotel, restaurant and catering industries as well as in construction, transportation and various business activities. In the tourism industry, Fiji leads the Pacific Island countries both in terms of numbers and earnings as illustrated by table 6. It can also be seen that earnings from tourism amounted to as much as 30 per cent of national exports in the case of Fiji and Tonga. Fijian authorities have estimated that tourist arrivals would reach 500,000 by the year 2000, bringing in earnings of $300 million and creating an additional 9000 jobs. Other Pacific Island countries are also aiming at a growth of around 6 per cent per year in their tourist industries.

The main tourist sources for the Pacific Island countries are Australia, United States, New Zealand and Japan, although South-East Asia and Canada are gaining importance as revealed in the category 'Other Countries'. Currently, Australia, United States and New Zealand contribute more than 60 per cent of tourist arrivals in the Pacific Island countries. It is perhaps a paradox that while being the main tourist sources, these three countries, backed by bigger marketing budgets and manpower resources, are also the main rivals of Pacific Island countries for the tourist dollar. However, the Pacific Island countries have been successful in attracting an increasingly larger number of tourist to the region, utilizing their inherent strengths of a natural unspoilt environment, friendly population, cultural attraction and good value for money.

The growth of the tourism industry has led to a mini-construction boom in some Pacific Island countries like Fiji, Tonga, Vanuatu and Western Samoa, where existing hotels are being extended and upgraded and new holiday resorts are being constructed in collaboration with foreign investors and hotel chains. Hotel resort planners and operators as well as capital from Australia, Japan, United States, New Zealand and South-East Asia are heavily involved in these devel-

opments. Besides the construction industry, wholesale and retail trades, restaurants, and other activities like transportation and tours also tend to benefit from the growth in the tourism industry.

Although there is significant local participation, the governments of most Pacific Island countries continue to offer generous incentives for the development of hotels and holiday resorts. The outflow of royalties, managerial fees, and other earnings to overseas hotel operators and chains is relatively free of restrictions which is an additional incentive for tourist development in the area. Given the proper marketing and planning, the tourism industry could certainly grow and would be able to withstand competition from traditional and new competitors. The establishment of the Tourism Council of the South Pacific in 1989 has given the Pacific Island countries a new capability to initiate and implement regional tourist development and marketing programmes which will help to consolidate their national efforts. Tourism is their key services sector, and in most cases, the catalyst of future economic growth.

Due to their geographical locations, the viability of tourism in the Pacific Island countries is dependent to a large degree upon the services of international airlines that operate to and from the source countries to the Pacific Island countries. International airlines from Australia, New Zealand and the United States tend to dominate the carriage capacity. Although most of the Pacific Island countries have their own national airlines, they operate small jet and turboprop aircraft and, with the exception of Air Pacific (Fiji) and Air Nuigini (Papua New Guinea), they do not operate beyond the region. Rationalization of air services between North America, Japan and Australia, and New Zealand has led to reduction in their en-route touch downs at the Pacific Island countries. This has not helped to increase tourist numbers from North America and Japan, as tourists who wish to go to the Pacific Island countries would need to fly on to Australia and New Zealand to reconnect for their final destinations. The withdrawal of Japan Airlines and Continental from Nadi in 1988, for instance, has adversely affected tourist arrivals from Japan, Canada and the United States to Fiji and other Pacific Island countries.

Transport, especially shipping and aviation, is a crucial sector to the Pacific Island countries although its contributions to their econo-

mies is not as significant as that of tourism. In terms of international transactions as shown in table 7, the Pacific Island countries spend more than they receive on shipment, passenger services and other transportation charges. This is mainly due to the fact that national transportation is relatively underdeveloped and their services meet strong foreign competition. Moreover, transport links operated by foreigners have generally been tailored to the operators' rather than the Pacific clients' needs. Airline links tend to radiate out from the major metropolitan countries. While services from such places as Sydney, Auckland and Honolulu to most of the Pacific Island countries are regular and relatively frequent, inter-Pacific country connections are scarce and usually involve circuitous routes.

In order to overcome some of the problems, most Pacific Island countries now have their own national airline but they have still to make an inroad into the most lucrative aviation sector in the Pacific region which is between Australia and New Zealand. This sector is presently dominated by Air New Zealand and Qantas which have fifth-freedom rights in the Pacific Island countries that allow them to pick up passengers in the Pacific Island countries and take them to North America and Asia. Pacific Island countries' airlines such as Air Pacific, Polynesian Airlines and Air Nuigini have only terminating rights in Australia and New Zealand. There is a long way to go, for instance, before Polynesian Airlines has all rights on an Apia-Auckland-Melbourne service or for Air Nuigini to operate a Port Moresby-Sydney-Christchurch service.

The increasing availability of suitable jet aircraft and upgradings of airports in the Pacific region have raised the possibilities for the Pacific Island countries to build a more wide-ranging network and to compete more effectively with the establishment airlines. With increased aviation activity, some Pacific Island countries like Fiji have found a niche in the aircraft servicing and catering market. Unlike previously, when practically all commercial aircraft used to be serviced in Australia, New Zealand or the United States, maintenance services are now provided in Fiji for other Pacific airlines.

The Pacific Island countries have been operating a regional shipping line since 1978, known as the Pacific Forum Line which is

structured as a limited liability company with the governments of Fiji, Kiribati, New Zealand, Papua New Guinea, Nauru, Solomon Islands, Tonga, Tuvalu, Western Samoa, and the Cook Islands as shareholders. The line operates four ships providing regular services between Australia and New Zealand ports and Micronesia, Melanesia and Polynesia. The Pacific Forum Line faces strong competition from other lines that operate the trans-Pacific routes. Japanese, Taiwanese and Chinese shipping companies are particularly active in the region. Internationally, the Pacific Island countries are substantial consumers of shipping services as can be seen from table 7. While efforts are being made to increase their share of shipping business in the Pacific area, the Pacific Island countries presently do not have ships operating to Asia, Europe or North America, the main origins and destinations of Pacific Island countries' imports and exports.

Opportunities exist particularly with the containerization of cargo and the tendency for ocean-going ships to make fewer port calls and to minimize the time spent in those ports. Domestic shipping operators could find more demand for services to ports in the region which are no longer ports of call for the intercontinental shipping lines. Trans-shipment and feeder services would be required to supplement the network, and break-bulk facilities would become a necessity at the main ports of call. In taking advantage of this trend, some Pacific Island countries like Fiji are making conscious efforts to generate more traffic by offering competitive rates to get shippers to use its facilities to trans-ship cargo, and thus become the trans-shipment centre for the Pacific Islands. Wharf equipment and storage facilities are being upgraded to improve overall efficiency and user satisfaction. In Western Samoa, Apia port is being improved to cater for increased container traffic. It is envisaged that by the year 2000 the container cargo for Western Samoa would comprise 81 per cent of imports and 70 per cent of exports. All these developments involve foreign assistance and due to the specialized nature of the exercise, foreign companies tend to be employed for the work.

In internal transportation, aviation and shipping figure prominently in most of the Pacific Island countries which are mostly chains of islands spaced over a wide expanse of the Pacific Ocean. Highway development is not yet advanced and rail services are non-existent. The

development of the aviation industry in the region has however caused problems for inter-island shipping operators who are mostly local nationals. The loss of passengers and freight to domestic air traffic has aggravated the problems caused by low volumes over vast distances. The increase in domestic air services for instance in Vanuatu to 27 destinations by Air Melanesie and by Talair in Papua New Guinea which now covers 160 locations has tended to make local travellers select air travel over sea-services in view of the travelling time saved. Yet inter-island shipping companies rely heavily on passenger traffic to supplement the income from carrying cargo. This has resulted in irregular sailing schedules with quantities of products in the outer islands unable to reach internal and external markets. The Pacific Island countries authorities are taking various measures to overcome the problems, such as investing in new fuel-efficient vessels, which are suited to the special nature of Pacific inter-island trade, increased infrastructures, better management and new incentives for shipping operators.

Together with the progress made in transportation, the Pacific Island countries are also engaged in efforts to improve telecommunications services which are essential to the main sectors of their economies such as tourism, fisheries, and business services. The demand for telephones and other telecommunications services has been growing steadily with the rise in living standards and increased international contacts. In the Pacific Island countries, telephone services have traditionally concentrated on urban centres, although the bulk of the population live in the rural areas. The governments have identified satellites as the preferred technical solution for providing links between rural areas and the capital cities as well as with international centres. The recognition of the role of telecommunications in breaking down the social and economic divisions between urban elites and the rural poor and in encouraging investment and development has resulted in various national efforts aimed at updating and extending the respective telecommunications networks in the Pacific Island countries. Australian, Japanese, United States and European suppliers of telecommunications technology are searching out for new business in the region which currently has only between 1 and 8 telephones for every 100 inhabitants.

The governments of the Pacific Island countries have begun to review their existing organizational arrangements with carriers such as Cable and Wireless which operates the international services of Fiji, Solomon Islands, Tonga, Vanuatu, and the Cook Islands. The Australian Overseas Telecommunications Commission (OTC) is actively bidding to manage or operate networks on a joint venture basis with Pacific Island countries. So far the OTC has signed up with Kiribati, Nauru, the Marshall Islands and the Cook Islands who have been promised cheaper satellite time through OTC's Demand Assigned Multiple Access (DAMA) System, centered at Sydney. The Australian government through its aid programmes is helping to upgrade satellite ground stations in the Pacific Island countries to fit in with the DAMA system. However, some countries, like Papua New Guinea, Fiji and Solomon Islands have opted to remain with existing partners as they are reluctant to see control from Sydney over their national and international circuits.

Telecommunications could in the years ahead become increasingly important in the services sector of the economies of the Pacific Island countries, especially in job creation and in opening up new fields of business such as computer networks, electronic mail, high-speed data transmission and tele-conferencing. Some Pacific Island countries are already planning their deep involvement for the next stage of development to ensure national sovereignty and control over the satellite facilities. Papua New Guinea for instance has a joint-venture agreement with a United States concern to launch a satellite using the Pacstar system. It has leased capacity from an Indonesian satellite to meet immediate requirements.

Other Pacific Island countries have found new possibilities for foreign-exchange earnings from satellite communications. Tonga, for instance, through a newly formed government-owned company has registered a number of satellite-orbit positions. It intends to collect fees from entities who need a satellite in one of these positions. Kiribati has offered one of its many islands to Japan for satellite launchings.

The Pacific Island countries have relatively well-developed banking services being provided by both local and foreign banks with the latter dominating the international transactions. Australian and new Zealand banks are active in all the Pacific Island countries. In the case

of Kiribati and Tuvalu, an Australian bank is the sole joint-venture partner with the governments of these two countries and their national banks. Most Pacific Island countries have at least one wholly locally-owned bank or a number of joint-venture banks with local interests holding a substantial share and partners from Australia, New Zealand and the United States. Like most other countries, banking licenses are controlled and local participation advocated.

Table 8 shows the distribution of commercial banks in the Pacific Island countries. Recent bank reports from the region indicate that the banking sector continues to grow at a healthy rate in comparison with the general economic trend. The Bank of South Pacific reported a good year (1988) in Papua New Guinea with after-tax profits of Kina 2.12 million compared to Kina 1.34 million in 1987. Bank income grew by 25.4 per cent, while deposits and loans grew by 12 per cent and 18 per cent respectively. The Bank of Western Samoa in its latest report showed a 23 per cent rise in deposits for that year. After-tax profit almost doubled to Tala 1.87 million over the previous year.

The relatively small population numbers in the Pacific Island countries and the limitations on lending to public and private sectors have led to some banks investing overseas. The Bank of Kiribati in 1988 invested 24.3 million Australian Dollars overseas out of a total asset base of 32.13 Australian Dollars. The Bank of Tuvalu had 6.18 million Australian Dollars out of its 9.06 million Australian Dollars total assets on term deposits in overseas banks. The main private-sector credit operations of commercial banks consist of short-term business financing, especially of foreign trade, longer-term loans for the purchase of capital equipment and investment goods in agriculture, tourism and industry. Development banks have been established by governments in most Pacific Island countries with government funds and loan finance from the World Bank and the Asian Development Bank to provide a cheaper source of funds for lending to industrial and agricultural projects. Overall banking prospects seem bright, particularly with tourism on the rise in the region, and foreign banks have been encouraged to expand their network into other population centres outside the capital cities.

The development of the banking sector has encouraged some Pacific Island countries to venture into the creation of offshore banking and international tax-free finance centres particularly to attract international investors and corporations seeking a tax haven. Vanuatu, Western Samoa and the Cook Islands provide such facilities, and responses have been particularly good in the case of Vanuatu and Western Samoa, as these countries were prepared to offer the necessary infrastructures and legislations to back up their financial centres. The establishment of such centres had also attracted to the trust companies, insurance, legal and accounting firms of those countries providing a range of specialized services and creating employment for the local population. In the case of Vanuatu, the financial centre and its related activities contributed about 10 million dollars to the national economy in 1987. This was equal to a third of the country's exports for that year. As at 1989, there were 758 tax-haven companies registered in Vanuatu employing 300 local staff.

Western Samoa's financial centre began operating in 1989 and it is understood that 30 companies had already registered with the authorities under the tax haven legislation. Efforts are being undertaken in Hong Kong, Hawaii and Mexico to promote the centre. Recent action by Australian and New Zealand governments in changing their tax laws to prevent their nationals taking advantage of tax havens has affected enquiries from these two countries, but other countries in Asia, Europe and North America would remain the main sources for registrations and expansion.

In addition to being a tax haven, Vanuatu operates an open registry for shipping which by the end of 1988 had 206 ships and was earning 200,000 dollars annually in fees. Recent political developments in competing countries such as Panama have led to a surge in transfers to Vanuatu registrations by Hong Kong, Taiwanese and Japanese ship-owners.

Some Pacific Island countries have taken advantage of their population numbers to export skilled and unskilled manpower to neighbouring countries as well as providing crews for shipping lines. Fiji, Tonga, Western Samoa, Kiribati, Tuvalu and Vanuatu have sizable numbers of their nationals working abroad and remitting back foreign-exchange earnings. Kiribati nationals are mostly employed in the

phosphate mine in Nauru and on ocean-going vessels of foreign shipping lines. Nationals from the other mentioned countries are mainly engaged in various employment in New Zealand, Australia, New Caledonia and North America. As table 9 shows, earnings from overseas employment are substantial. It is estimated that remittances from overseas employment in Tonga is about three times that of the country's merchandise exports while in Western Samoa, it is about twice the merchandise exports figure. For Kiribati and Vanuatu, the proceeds from overseas employment amount to about 40 per cent and 20 per cent of their merchandise exports respectively. It is perhaps worth noting that amongst the Pacific Island countries, Kiribati, Solomon Islands and Nauru engage a sizeable amount of foreign labour. In the case of Kiribati and Solomon Islands, most of the specialized educational, medical and technical services are run by expatriates while in the case of Nauru, in addition to these services, foreign labour especially from Kiribati and other Pacific Islands are engaged in phosphate mining.

Increasing contacts with the major economic powers and closer involvement with world issues have given the population of the Pacific Island countries a wider and deeper exposure to opportunities in the Pacific area and beyond. With the development of modern modes of transportation, the opportunity for labour mobility has increased in the region and there is a growing tendency for longer duration and distance labour migration which could become the general feature in the years ahead, beginning with migration to the metropolitan countries on the fringes of the Pacific.

Improved communications and frequent contacts with the international community have led to the rapid deployment and absorption of new office technology and equipment like computers and facsimile machines. However, the suppliers of the equipment and services are mostly foreign (Australian and New Zealand) owned firms which hold the exclusive marketing rights in the Pacific area. Several business organizations have been established to provide training on the use and servicing of new office equipment and software. Chambers of Commerce and Manufacturers' Associations are present in all of the Pacific Island countries and with the assistance of international organizations, are providing information and training to local business enterprises in

export development and trading skills. The promulgation of various incentive schemes for industrial and trade development in several Pacific Island countries has spawned the growth of local business and industrial consultants to cater for the needs of foreign investors who hitherto were using expatriate accountants and law firms in their dealings with the government agencies.

The growth in business activities and tourism in the Pacific Island countries has also seen the introduction of charge card and credit card facilities. Almost all of the internationally known cards are in use in the region with Australian banks being the main operators. Due to the relatively tight local credit control exercised by the financial institutions, the number of local card holders is small when compared to other regions. However, retail outlets, especially hotels and restaurants, accepting these cards are sizable in number arising from the need to service foreign tourists.

Insurance services are quite well developed in the Pacific Island countries with the clientele coming from business enterprises and people located in the urban centres. The rural sector is comparatively uncovered by insurance. Practically all the insurance business is written by Australian and British owned insurance companies which have established branches in the Pacific Island countries. Besides these foreign owned branches, an Indian owned company and a partially Fijian owned one also operate in Fiji.

IV. URUGUAY ROUND AND TRADE IN SERVICES OF PACIFIC ISLAND COUNTRIES

There is already abundant UNCTAD literature on the Uruguay Round and the current state of play in the negotiations on trade in services.[1] This section will not address the general aspects of the negotiations, but will focus on areas of importance to the Pacific Island

1 See, for example, *Uruguay Round: Papers on Selected Issues* (United Nations Publication, UNCTAD/ITP/10), *Uruguay Round: Further Papers on Selected Issues* (United Nations Publication, UNCTAD/ITP/42), *Services and Development Potential: The Indian Context* (United Nations Publication, UNCTAD/ITP/22), and *Trade in Services: Sectoral Issues* (United Nations Publication, UNCTAD/ITP/26).

countries. Trade in services provided by the Pacific Island countries is influenced by a number of international arrangements and agreements including sector-specific ones. These arrangements mainly cover aviation, maritime transport and telecommunications. They include the Convention on International Civil Aviation, the International Air Transport Association, the Convention on Facilitation of International Maritime Traffic, the Code of Conduct on Liner Conferences, the International Telecommunications Convention and the International Telecommunications Satellite Organization (INTELSAT). These arrangements are mostly aimed at elaborating technical standards, legal and administrative matters and, in some cases, market allocations.

The Uruguay Round is the first round of multilateral trade negotiations to include trade in services and to attempt to formulate a multilateral framework of principles and rules to cover international trade in services. Recent interest in international trade in services seemed to have arisen from three main factors, namely:

- Technological changes that have facilitated easier and cheaper communications and transport facilities;
- Deregulation measures which are opening up service markets for local and foreign firms; and
- The tendency for countries where domestic service activities make up a large part of their economy to seek opportunities to market those services in other countries, possibly in response to the reduced scope for expansion of traditional and manufactured exports and in recognition that services account for increasing share of value-added in manufacturing and are a determining factor in international competitiveness.

These factors have brought about considerable pressure on trade-policy markers and business in many countries including the Pacific Islands, despite the fact that they are not actively engaged in the Uruguay Round negotiations.

Negotiations in the GNS seem to indicate that the intention of a trade in services framework agreement is to progressively liberalize

market access for foreigners subject to certain principles and rules, including transparency, non-discrimination and national treatment.

The principle of transparency requires governments to make their interventions visible. The Mid-Term Review text specifies that the ultimate agreement should ensure the availability of signatories of information concerning all laws, regulations and administrative guidelines as well as information on international agreements relating to services trade to which the signatories are parties. While it may seem quite straightforward for some countries, a commitment of this nature will pose severe administrative and financial strain on most Pacific Island countries, the government machineries of which are already strained by the regular tasks. Special consideration in terms of time period for compliance and technical assistance should be provided for Pacific Island countries and other developing countries in a similar situation.

The principle of non-discrimination requires a signatory to make available to all signatories any concession granted to one signatory. The Mid-Term Review text specifies that the multilateral framework shall contain a provision on most-favoured-nation/non-discrimination. However, the precise content of this rule is being negotiated. While the principle could generally be effected by Pacific Island countries, there may be need for a phase in period in the light of possible future developments in the South Pacific Forum, the Melanesian Spearhead Movement and Polynesian Co-operation. It appears that the multilateral framework will provide for such regional co-operation among developing countries.

The Mid-Term Review text defines "national treatment" to mean that the services exports and/or exporters of any signatory are accorded in the market of any other signatory, in respect of all laws, regulations and administrative practices, treatment no less favourable than that accorded to domestic services or services providers in the same market. In the light of the low level of local participation in some of the service trade, the Pacific Island countries would need flexibility in respect of including national treatment in their commitments. As in the case of many developing countries, certain services sectors like wholesale and retail in some Pacific Island countries are closed to foreigners in order to promote indigenous participation.

Another contentious issue linked to "national treatment" is whether market access should include the "right of establishment", i.e. the right of any foreign competitor to establish a commercial presence in a market. Some developed countries have argued for the inclusion of the right of establishment (or "commercial presence") in a framework agreement, but developing countries have been opposed to it. Pacific Island countries are no different from other developing countries under the circumstances.

Another issue of significance to Pacific Island countries is the proposal by developing countries for the inclusion of provisions to allow full temporary movement of labour. Developed countries have generally sought to confine such provisions to certain categories of essential skilled personnel which many developing countries, including the Pacific Island countries, would be in no position to provide. In view of the relatively high remittances to the economies of some Pacific Island countries, there is need to pursue this proposal vigorously in order to expand opportunities in this sector. The most recent trend in the negotiations is to provide for "commerical presence" as a market-access commitment.

The question of sectoral coverage is being considered in the GNS. As the Mid-Term Review text states that no sector is to be excluded at the outset and as the majority of developed and developing countries favour universal coverage, it would not be unreasonable to presume that the sectors of importance to the Pacific Island countries, especially tourism, aviation, shipping, telecommunications, banking and finance, business services and manpower services would be covered.

As described in Section III, most of these sectors have potential for further development given the right environment. The fragility and vulnerability of the Pacific Island countries' economies make it necessary for certain regulations to be promulgated, which tend to affect trade and services. However, not all of these regulations are motivated by the desire to exclude foreign competitors. In many instances, they are made to protect the local population from the strategic and cultural viewpoints. Hence sectoral service agreements are equally important for the Pacific Island countries, and their involvement in the GNS working groups would be useful.

V. CONCLUSION

The services sector is the largest part of the economies of most Pacific Island countries and is growing at a healthy rate. There are specific sectors which have substantial growth potential and some with export potential, but limitations posed by the size of national economies, geographical distance, and the availabity of finance and skills should be recognized. A complete opening of the various service sectors in the Pacific Island countries could create problems, but at the same time liberalization in cross-border transfers of services cannot be avoided and could be of advantage, especially when there is a heavy reliance on tourism in many of the countries.

There is need for the special problems of the relatively small and geographically remote island countries to be recognized in the negotiations. Participants of Pacific Island countries at the Seminar on Developments in the Uruguay Round of MTNs held in Suva 4-6 April 1990 had stressed the importance of trade in services to the realization of the development potential of their countries, particularly taking into account the present developments in telecommunications, tourism and transport in the region.

The Pacific Island countries, in not having a direct negotiating role in the Uruguay Round and the GNS, have missed some of the opportunities to put their views for consideration. Hence it would seem essential for Pacific Island countries to be actively involved in the remaining stages of the negotiations in the GNS and especially the specific sector negotiations of importance to them, including those which may take place after agreement is reached on the multilateral framework. With the services sector providing the mainstay and growth potential for their economies, the Pacific Island countries should not only be involved in the negotiating stages but also in the implementation of the results so as to strengthen their tradable services. This could perhaps best be performed through a special project of technical assistance for the Pacific Island countries, which could also assist them in ensuring that they draw full benefit from the results of the Uruguay Round negotiations on trade in services.

Table 1

SALIENT ECONOMIC INDICATORS, 1986

Country	*Population (thousands)*	*GNP per Capita at market prices (dollars)*	*Exports (million dollars)*	*Imports (million dollars)*
Fiji	715	1,800	247	379
Kiribati	65	500	5	15
Nauru	9	11,000	72	33
Papua New Guinea	3,390	690	1,029	858
Solomon Islands	282	540	67	63
Tonga	95	690	5	40
Tuvalu	8	680	0.02	2
Vanuatu	140	1,120	30	70
Western Samoa	161	680	14	50

Source: South Pacific Commission and National Statistics.

Table 2

RELATIVE IMPORTANCE OF SERVICES IN GDP, 1970/1985

	Distribution of GDP (per cent)					
	Agriculture		*Mining & industry*		*Services*	
Country	*1970*	*1985*	*1970*	*1985*	*1970*	*1985*
Fiji	25	21	21	12	44	67
Kiribati	13	27	42	2	45	71
Nauru	na	na	na	95	na	5
Papua New Guinea	37	33	22	20	41	47
Solomon Islands	na	49	na	6	na	46
Tonga	47	22	9	10	35	68
Tuvalu	na	14	na	2	na	84
Vanuatu	na	34	na	4	na	62
Western Samoa	50	34	7	15	43	51

Source: South Pacific Commission and National Statistics; United Nations "National Accounts Statistics"; Commonwealth Secretariat.

Table 3

DISTRIBUTION OF LABOUR FORCE, 1986

Country	*Total Employed Labour force (thousands)*	*Percentage of labour force in*		
		Agriculture	*Mining & industry*	*Services*
Fiji	248	46	17	37
Kiribati	7	73	4	23
Nauru	3	-	86	14
Papua New Guinea	215	76	10	14
Solomon Islands	140	32	9	59
Tonga	24	51	9	40
Tuvalu	4	4	1	95
Vanuatu	60	79	3	18
Western Samoa	43	67	8	25

Source: South Pacific Commission and Commonwealth Secretariat.

Table 4

SELECTED BALANCE-OF-PAYMENTS STATISTICS, 1986
(million dollars)

	Exports of goods and NFS			*Imports of goods and NFS*		
Country	*Merchandise*	*Services*	*Total*	*Merchandise*	*Services*	*Total*
Fiji	243	289	532	367	141	508
Kiribati	1	12	13	12	7	19
Nauru	na	na	na	na	na	na
Papua New Guinea	1,027	72	1,099	925	301	1,226
Solomon Islands	66	18	84	67	51	118
Tonga	5	15	20	35	12	47
Tuvalu	na	na	na	na	na	na
Vanuatu	9	30	39	47	29	76
Western Samoa	10	13	23	43	13	56

Source: IBRD, "Trends in Developing Economies 1989".

Table 5

SERVICES AS PERCENTAGE OF TOTAL EXPORT AND IMPORT OF GOODS AND NON-FACTOR SERVICES 1986

Country	*Services as per cent of total*	
	Export	*Import*
Fiji	54.3	27.8
Kiribati	92.3	36.8
Nauru	na	na
Papua New Guinea	6.6	24.6
Solomon Islands	21.4	43.2
Tonga	75.0	25.5
Tuvalu	na	na
Vanuatu	76.9	38.2
Western Samoa	56.5	23.2

Source: IBRD, "Trends in Developing Economies 1989".

Table 6

TOURIST ARRIVALS AND EARNINGS, 1975/1988

Country	*Tourist earnings (million dollars)* 1975	*1988*	*Current tourist earnings as per cent of exports*
Fiji	75.0	176.0	30
Kiribati	na	na	na
Nauru	na	na	na
Papua New Guinea	na	13.0	1
Solomon Islands	na	2.4	3
Tonga	na	12.0	30
Tuvalu	na	na	na
Vanuatu	na	14.0	17
Western Samoa	5.0	7.0	25

Source: Tourism Council of the South Pacific and the Commonwealth Secretariat.

Table 7

INTERNATIONAL TRANSPORT TRANSACTIONS, 1986
(Million SDRs)

	Shipment		Passenger services		Other transportation	
Country	*Credit*	*Debit*	*Credit*	*Debit*	*Credit*	*Debit*
Fiji	1.30	-43.20	19.60	-7.80	35.60	-2.90
Kiribati	0.30	-3.00	0.93	-0.46	0.59	-1.69
Nauru	na	na	na	na	na	na
Papua New Guinea	8.10	-101.90	11.50	-36.30	-	-
Solomon Islands (1984)	-	-12.90	0.80	-2.30	4.70	-8.80
Tonga	0.61	-4.88	-	-	1.62	-1.20
Tuvalu	na	na	na	na	na	na
Vanuatu	-	-7.90	-	-1.90	3.60	-
Western Samoa	0.01	-3.61	0.80	-1.22	1.21	-0.64

Source: IMF Balance of Payments Statistics 1988

Table 8

COMMERCIAL BANKS IN OPERATION 1990

Fiji	4
Kiribati	1
Nauru	1
Papua New Guinea	6
Solomon Islands	3
Tonga	1
Tuvalu	1
Vanuatu	4
Western Samoa	4

Source: South Pacific Forum Secretariat.

Table 9

LABOUR INCOME AND WORKER REMITTANCES
(Million SDRs)

Country	*Year*	*Credit*	*Debit*
Fiji	1986	5.9	-
Kiribati	1986	1.8	-1.4
Nauru	na	na	na
Papua New Guinea	na	na	na
Solomon Islands	1985	-	-2.5
Tonga	1987	16.5	-2.1
Tuvalu	na	na	na
Vanuatu	1986	5.9	-0.6
Western Samoa	1987	28.3	-0.1

Source: IMF, *Balance-of-Payments Statistics, 1988.*

THE MAIN ISSUES IN THE NEGOTIATIONS OF A MULTILATERAL FRAMEWORK FOR TRADE IN SERVICES

*Murray Gibbs and Mina Mashayekhi**

A. State of play

Since the Uruguay Round Mid-term Review of December 1988 which laid out the basic principles for a multilateral framework for trade in services, the Group of Negotiations on Services (GNS) has examined the application of these principles to several sectors and has attempted to draw up a text of a multilateral framework for trade in services. The Group has before it various submissions in the form of draft legal texts submitted by various countries, including one by 11 Latin American countries, and another by seven other developing countries, including from the Asia and Pacific region. The Chairman of the GNS presented a "profile" of a draft multilateral framework for trade in services to the GNS and the Trade Negotiations Committee (TNC) on his own responsibility in July 1990.

The report of the Chairman of the GNS to the TNC in July took the form of a "profile", i.e. a draft text for the framework, containing the main substantive provisions with few square brackets, although it was made clear that the entire text was subject to further consideration, and that certain outstanding issues would have to be resolved if negotiations were to progress further. When the negotiations resumed in late August, the GNS decided to target completion of work on a full text of a multilateral framework of principles and rules with possible annotations for individual sectors to be made available for consideration by 21 November 1990.

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At the time this volume goes to print, the Uruguay Round negotiations of a multilateral framework for trade in services are in their final stage, the sectoral working groups are scheduled (see discussion below) to terminate their work on 20 October 1990, so that a draft multilateral framework agreement - accompanied by sectoral annotations, where necessary, and by schedules of concessions, if possible - can be submitted for the approval of Ministers at the final meeting of the TNC to be held in Brussels beginning 3 December 1990.

The following paragraphs summarize some of the most important of the current issues which will have to be resolved if these negotiations are to be successful, from the point of view of developing countries, including those of the Asia and Pacific Region.

B. Structure of the multilateral framework agreement

The overall structure of the multilateral framework has become a question of crucial importance. There would seem to be an emerging consensus that the structure of the agreement would be such as to clearly delineate general obligations that would be accepted by all parties upon their signature of the framework (e.g. most-favoured-nation treatment, increasing participation of developing countries, transparency, etc.) separately from the market-access commitments (including national treatment) which would be the subject of specific negotiations, and included in each signatory's schedule of concessions. This is considered essential by developing countries, as it would mean that their acceptance of the framework would not imply their having to provide access in any particular sector. That would be the subject of negotiations with interested countries in which access commitments could be offered with respect to those sectors or subsectors where liberalization would be consistent with their development strategies and in return for meaningful access to developed-country markets (see below). The general obligations could include provisions relating to most-favoured-nation treatment, transparency, increasing participation of developing countries in world trade in services, subsidies, monopolies, anti-competitive practices, etc., although obligations with respect to some of these issues might be applied only to sectors where a specific access commitment had been made.

C. Scope/Definition

The Montreal principles specified that the multilateral framework may include trade in services, including cross-border movement of service consumers and of factors of production (however, in the latter case when occuring "under conditions of specificity of purpose, discreteness of transactions, and limited duration", thus reflecting the views of developing countries that immigration and investment would not be covered, i.e. not acceptable as subjects of concessions. It is clear, however, that for many services, developed countries will be seeking concessions with respect to "commercial presence", where this is necessary to deliver a service effectively to foreign markets. Developing countries have argued that factors of production are to be treated symmetrically in the framework and in the negotiations, i.e. that services delivered through the movement of persons should not receive a less degree of liberalization than those involving capital flows.

With respect to the scope of the framework, developing countries have maintained that all tradable services should be covered, a position shared by the European Community and most developed countries. However, the United States and some others, in response to domestic political pressures, have taken the position that countries could have the right to exclude sectors. If exclusions were to be permitted, it would be likely that each participating country would exclude those sectors where strong political opposition to liberalize existed, rendering the multilateral framework virtually meaningless.

D. Most-favoured-nation treatment

The preservation of the unconditional most-favoured-nation principle is seen as essential by all the proposals made by developing countries as well as by most proposals from developed countries. As noted below, some proposals by the developed countries, related to sectoral annotations appear aimed at qualifying the MFN obligation in certain sectors and even permitting special limited agreements applied on a conditional basis in others. The problems some countries face regarding the coverage of certain sectors within the framework as a whole may be related to the application of this principle. Any quali-

fication of the unconditional MFN clause is strongly opposed by developing countries.

There would seem to be recognition that regional integration arrangements could provide for a greater degree of liberalization than that extended on an MFN basis, and that provision would be made for preferential agreements among developing countries, as well as preferences in favour of developing countries. The possibility of "grandfathering" existing arrangements and ways of treating existing international agreements dealing with services is a matter being discussed in specific sectoral contexts.

E. Increasing participation of developing countries

That the multilateral framework provide for the increasing participation of developing countries in world trade in services, the expansion of their services exports, the strengthening of their domestic services capacity and for extending them effective access to markets was recognized at the Montreal Mid-Term Review. The question has arisen as to how such provisions can be incorporated into the framework as legally binding obligations. Developed countries have argued that these endeavours should take the form of preambular phrases or declarations of intent but not contractual obligations. Developing countries have recalled that at Punta del Este it was clearly recognized that the development of developing countries was one of the primary objectives of the framework. The framework should therefore provide for concrete measures to achieve the above-mentioned objectives, both by the developing countries themselves, and by developed countries who clearly dominate world trade in services.

The inclusion in the general obligations of the framework of clear principles on the increasing participation of developing countries is seen as essential in order to remove any doubt regarding the legitimacy of measures taken by developing countries to strengthen their services capacity and their ability to penetrate world markets. Such measures include stipulating conditions relating to transfer of technology and training or access to information networks and distribution channels to foreign service suppliers benefiting from market-access concessions. These general obligations should also recognize that developing coun-

tries will need to apply other national policy measures for this purpose, including the possibility to subsidize their services sectors.

Developing countries have also sought that developed countries accept concrete obligations to provide developing-country service suppliers with effective access to markets. As the export potential of many developing countries depends largely on the liberalization of cross-border movement of personnel covering the entire spectrum of skills from unskilled or semi-skilled to high-skilled professionals, developing countries have sought recognition that the developed countries should liberalize their national regimes so as not only to enable developing-country firms supplying services abroad to recruit personnel from their own domestic sources, but also to permit service firms to recruit personnel from the source which is economically most advantageous. The specific measures proposed include: (a) establishment of enquiry and contact points to provide exporters from developing countries with commercial information, and to assist developing-country exporters with questions relating to registration, recognition and completion of professional qualification, obtaining such qualifications in cases of lack thereof; (b) grant of preferential market access to exports and/or exporters of services from developing countries; (c) prohibition of measures and practices that limit or impede access to information networks and distribution channels for services; (d) elimination of measures that impede or limit free choice in the acquisition of technologies, as well as those that restrict access to such technologies; (e) facilitation of training programmes for local personnel and the exchange of personnel of developing countries; (f) promotion of the participation of national suppliers from developing countries in the research and development activities conducted by foreign suppliers.

F. Domestic regulation

The Punta del Este Declaration stated that "the framework shall respect the policy objectives of national laws and regulations". Developing countries have stressed the importance of their being allowed the flexibility necessary to pursue effectively their national policy objectives. Developing-country proposals on regulatory situation follow the Punta and Montreal mandates in providing that parties to the framework shall have the right to regulate the provision of services within their territo-

ries, *inter alia* through the grant of exclusive rights in certain sectors, in order to implement national policy objectives.

G. Monopolies and exclusive service providers/behaviour of private operators

Some developed countries have sought strict rules with respect to the operation of monopolies which may extend even beyond the scope of the schedules of commitments. On the other hand, to different extents, developed countries have resisted comparable provisions with respect to the treatment of RBPs and other anti-competitive practices of private corporations. Developing countries fear that if the framework were to contain weak provisions in this repect, it would be interpreted by enterprises as a clear indication of the lack of determination by governments to deal with anti-competitive practices. Thus, developing-country proposals aim at imposing obligations on all parties to take all possible measures, by legislation or otherwise, to ensure, within their jurisdiction, that service suppliers do not engage in unfair trade practices, to establish international standards and disciplines for the control of adverse trade effects of anti-competitive private sector behaviour, and to create a multilateral mechanism to enforce such standards and disciplines. The prevalence of anti-competitive practices has been noted elsewhere in this volume and in earlier publications under this Project.[1]

H. Subsidies

While developing countries may need flexibility in using subsidies to improve their domestic capacity for the production of services, they would have a clear interest in a total prohibition on subsidies by developed countries. Some developing-country proposals provide for a standstill and rollback on the subsidies of developed countries, while permitting flexibility for use of subsidies by developing countries to achieve the specific objectives of strengthening their domestic services

1 See P. Brusick, M. Gibbs, M. Mashayekhi, "Anti-Competitive Practices in the Service Sector", in *Uruguay Round: Further Papers on Selected issues* (United Nations Publication, UNCTAD/ITP/42), pp. 129-56.

capacity and achieving an increasing participation in world trade in services.

I. Negotiation of commitments/Progressive liberalization

While all parties to the Framework could accept the idea of the progressive liberalization of the adverse trade effects of laws, regulations and administrative practices, as provided in the Montreal text (paragraph 7 (b)), consistent with the structure of the Framework described above, specific liberalization commitments would be confined to those included in each party's schedule of concessions. The provisions on progressive liberalization would include market access, which could be defined in terms of the different modes of delivery and national treatment. Developing countries have stressed that the provisions for future liberalization should be based on a "positive list" approach. This would entail that liberalization would be achieved through the inclusion and progressive addition of sectors and subsectors to the schedules of concessions, indicating those for which parties would agree to provide market access and national treatment.

The "positive list" approach is seen as possessing clear advantages over a framework under which developing countries would be required to submit "reservations" with respect to sectors or transactions that they would not be prepared to liberalize immediately. This latter approach would imply that they would be immediately placed on the defensive, i.e. under pressure to liberalize access to their markets for services unilaterally, whether or not they were able to effectively benefit from the multilateral framework and from the liberalization by developed countries, in terms of increased exports and market penetration by developing-country enterprises. In fact, it could imply that parties would be accepting the fundamental "right of establishment" and of national treatment, while temporarily reserving their position with respect to the immediate application of such principles.

There are also fundamental technical reasons why developing countries have advocated the positive list approach. It would be impossible for most developing countries (which, unlike OECD countries, have not had decades of experience in this respect in the context of the relevant OECD instruments) to determine which laws, regulations and

administrative guidelines would come under the scope of the agreement and, thus (according to the negative list approach) be subject to market access and national treatment obligations unless reservations were made. This might also cause legal and constitutional problems as it would be extremely difficult to convince legislatures to apply such an agreement, given the serious but unclear implications for a wide variety of existing legislation. Also, faced with such a dilemma, most developing countries are likely to find themselves in a position of having to submit virtually blanket reservations, which would give rise to accusations that they were not making an acceptable level of commitment, and provoke resort to non-application clauses. Moreover, in future negotiations they would find themselves on the defensive, being submitted to a justification rather than bargaining process. Not only would this make it difficult for them to achieve reciprocity in future rounds of negotiations but could also provoke bilateral pressures (such as the "section 301" actions which have already been initiated) on the basis that the developing countries in question had maintained too many reservations or for too long.

J. Market access and national treatment

The structure of the framework could thus provide that market access and national treatment provisions are not obligations, but are to be exchanged as negotiated commitments, with respect to individual sectors or subsectors. Market-access commitments would be negotiated in accordance with the definition of trade in services, and foreign suppliers could be obliged to accept obligations as described above under increased participation of developing countries as a condition for access to markets, specifying that the modes of delivery would be individually negotiable. Market access should not be made dependent on reciprocal concessions within the same sectors so that parties could seek liberalization in those sectors and subsectors where they possessed comparative advantage and grant concessions in those sectors where liberalization was judged most compatible with their economic, social and development interests. Such an approach would mean that as was the case in goods under the GATT, negotiations could address those sectors where liberalization was less difficult and thus quickly consolidate the legal structure of the framework. Developing countries need to ensure that the framework does not provide for the recognition of any "right" to

market access and national treatment, but that developing countries' commitments with respect to market access and national treatment would be confined to those sectors and subsectors where they would agree to specific concessions, and that symmetry should be maintained between the treatment of movement of factors of production, i.e. capital and labour, associated with the supply of services.

K. Sectoral annotations

The Montreal Mid-Term Review recognized that sectoral specificities would have to be taken into account, and provided that before the concepts, principles and rules which comprise a multilateral framework for trade in services are finally agreed upon, these concepts, principles and rules will have to be examined with regard to their applicability and the implications of their application to individual sectors and to the types of transactions to be covered by the multilateral framework.

An initial examination of six service sectors (transport, telecommunication, construction, tourism, professional and financial services) at the GNS was held in 1989. In May 1990, the GNS decided to establish sectoral working groups to discuss sectoral specificities and to determine whether the particular characteristics of the sectors warrant a specific "annotation" in order to clarify the application of the general principles or to provide for certain derogations from them. Since June 1990, eight working groups have met on transport (air, sea and land), telecommunications, financial services including insurance, professional services, labour mobility, tourism, construction and engineering, and audio-visual services.

By 20 October 1990, the sectoral working groups are expected to give their assessment as to whether or not a specific annotation/annex is needed in that sector, in the light of any relevant characteristics or peculiarities identified by the working group in the sector under discussion. Should an annotation be needed, the groups are to identify the issues and provisions that should be annotated and suggest, to the extent possible, the nature and content of such an annotation in relation to the specific provisions of the framework involved. An open-ended *ad hoc* working group consisting of GNS negotiators and sectoral

experts would then take stock of the situation in the light of the conclusions reached in the working groups, and finalize the draft texts of annexes or annotations where these appeared necessary.

Both the initial examination and the working group deliberations have revealed certain common aspects, particularly the weakness of the position of developing countries due to financial, technological and infrastructural factors, and their need to pursue their national trade policy objectives and to enhance their national service capacity. The initial examination has also revealed their need to have access to technology, information networks, training facilities and finance; to have access for their temporary labour services in the markets of the developed countries; and to implement gradual liberalization, based on their national policy objectives and in light of the benefits they received. The discussions demonstrated considerable difference in the degree of applicability of principles to the sectors under consideration.

The idea of "sectoral annotations" is that these would accommodate the peculiar aspects of certain sectors in the application of the framework's general principles to their special circumstances. In the discussions in the sectoral groups different reasons have surfaced for the need for sectoral annotations. One of the most generally accepted reasons has been that of dealing with the particular technical characteristics of the sector which make it difficult to translate general concepts such as "market access", "national treatment" and "non-discrimination" into operative commitments. The most pertinent example of this is the telecommunications sector where such concepts will have to be translated into "telecom language" if the principles of the multilateral framework and specific access concessions are to be effectively implemented.

Another approach has been to seek sectoral "annotations" as a means of negotiating generally-agreed derogations from some of the multilateral principles. As has been discussed elsewhere in this volume, proposals to this effect have been made with respect to air transport (and other transportation services) and audio-visual services. Such annotations may also address the relationship of the Multilateral Framework to existing multilateral arrangements dealing with aspects related to trade in several service sectors.

A third approach aims at an "annotation" which would actually provide for liberalization obligations. Proposals with respect to the financial services sector come very close to a separate, self-contained agreement for the liberalization of trade in the sector - "self-contained" in the sense of containing a balance of mutual rights and obligations among signatories. The danger of such a proposal for the integrity of the overall framework is that it could lead to some signatories adopting a conditional approach, i.e. extending the benefits of liberalization only to those parties to the multilateral framework who accepted the obligations of the "annotation".

An additional motivation for sectoral annotations is to clarify the application of modes of delivery, such as telecommunications and the movement of persons, so as to ensure that access-to-markets concessions are not nullified.

The trend of the negotiations on air transport, professional services, tourism, audio-visual services, professional services, labour mobility, tourism and financial services have been discussed elsewhere in this volume. The following pages discuss the telecommunications sector, which is a special case for reasons which have been described above and where there appears to be a consensus that a sectoral annotation is necessary.

L. Telecommunications

The dual role of telecommunications as a service sector and a mode of delivery for many other services is now widely appreciated, deriving to a considerable extent from the insistence of developing countries on this point and the two joint submissions by several developing countries. The purpose of the separate submissions was to distinguish issues relating to the scope, coverage and sectoral peculiarities arising from the application of the multilateral framework to international trade in telecommunications services, from those pertaining to telecommunications as a mode of delivery. It also aimed at ensuring that the conditions of use of telecommunication services as a mode of delivery do not impair the market-access commitments made in schedules, taking into account the different levels of development as between developed and developing countries' existing telecommunication capa-

bilities, while at the same time clarifying that any such annotation should not result in liberalization in any sector, including telecommunications, without a negotiated commitment having been made. Moreover, it is to ensure that the use of telecommunications as a preferred mode of delivery should not imply that preferential treatment will be given to foreign entities in terms of regulations applied to a party's domestic users. Nor should it imply interference with a party's determination of the technologies and equipment which will be permitted to be imported via telecommunications or operated in the domestic market in terms of their compatibility with and suitability to local conditions.

Technical standards have been extensively discussed in the Working Group, and the necessity to promote international standards which are primarily established in the ITU in order to ensure global end-to-end compatibility and interoperability of telecommunications services were found essential. Standards also are recognized as important to ensure the safety, integrity and interconnection of telecommunications systems and equipment. Whether technical standards should be compulsory is an unsettled matter. For many developing countries, a single, universal standard for public services and the inter-connection of value-added services and leased lines are considered to be necessary, since a multiplicity of private, proprietary, equipment standards could entail costly redesign of public facilities, and provide special advantages to transnational service suppliers.

Developing countries, as well as developed countries, wish to be able to reserve certain services (often described as "basic" services, although the distinction between "basic" and "enhanced" appears difficult to apply in practice) from any access-to-markets provisions. Their motive is to protect telecommunications organizations from pressure to revise investment priorities for residential versus international business users, to permit different terminal equipment to be connected to public networks, and to amend domestic regulatory policy so as to satisfy demands from foreign suppliers for full access and use of telecommunication facilities.

Developing countries' participation in the telecommunications field could be increased by the allocation of financial and human resources to assist developing countries expeditiously in introducing improvements in their telecommunications infrastructures. The

submission of developing countries also encourages parties to agree to give priority to the telecommunications needs of developing countries through international lending institutions and the United Nations system. In terms of unilateral action, developing countries assert the right to cross-subsidize public telecommunications services from revenue derived from telecommunications services operators and users and may impose obligations on foreign suppliers of telecommunications services with respect to transfer of technology, training, provision of telecommunications equipment on concessional terms, location of data resources and data-processing facilities and access to information and distribution channels.

On pricing, the developed countries have proposed using cost-related basis. In view of the public-utility responsibilities of public telecommunications organizations in many developing countries - such as the provision of universal telephone service - the introduction of pricing rules will be highly disruptive to these goals. Any solution proposed should take into account the full range of responsibilities of public telecommunications organizations rather than simple cost-related issues.

M. General comments

Given the asymmetry in the competitiveness of developed and developing countries in the service sector, world trade in services being dominated by enterprises from developed countries which are particularly well-endowed with capital, technology and information, only a balanced outcome of the negotiations, respecting the positions of both developed and developing countries, would permit the developing countries to strengthen their service sectors and to acquire the ability to penerate world markets for services. A "balanced outcome" cannot be seen exclusively in terms of access opportunities in the form of liberalization of regulations, as developing countries will not have the means to deliver their services to foreign markets. A multilateral framework will have to be constructed so as to assist them in achieving these means.

Although the situation is very fluid, it can be said that, as the negotiations enter their final stage, the main objectives being pursued by developing countries are as follows:

- Market access, including national treatment, should be the subject of specific concessions based on a positive list approach.

- Trade in services should be defined as in the Montreal text, and should ensure the inclusion of all categories of "labour" and "labour-intensive services" as legitimate subjects for requests for access to markets as well as the symmetrical treatment of capital and labour in schedules of concessions.

- The principle of unconditional MFN/non-discrimination should be unqualified so as to preclude limited arrangements among "like-minded" countries applied on a conditional basis, outside the context of regional arrangements or preferential schemes among developing countries.

- Liberalization by developing countries in future rounds should take into account their actual export performance and not hypothetical market-access opportunities, and the negotiating mechanism should ensure that they are not required to make concessions incommensurate with the benefits they receive from the multilateral famework.

- Safeguard measures should permit developing countries to deal with adverse trade effects caused by situations of concentration of ownership, market domination and restrictive business practices; specific measures should be included in the framework to discipline anti-competitive behaviour of market operators and a multilateral mechanism should be agreed upon to enforce such disciplines.

- The objective of increased participation of developing countries should be pursued jointly by all parties. Foreign service suppliers benefiting from concessions negotiated under the framework should accept conditions with respect to transfer of technology, training, and access to their information networks and distribution channels as conditions for access to the market. In addition, de-

veloped countries should take positive action in order to ensure that developing countries achieve effective access to their markets.

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